Senate Budget and Fiscal Review

Subcommittee No. 4, 2011 Agendas

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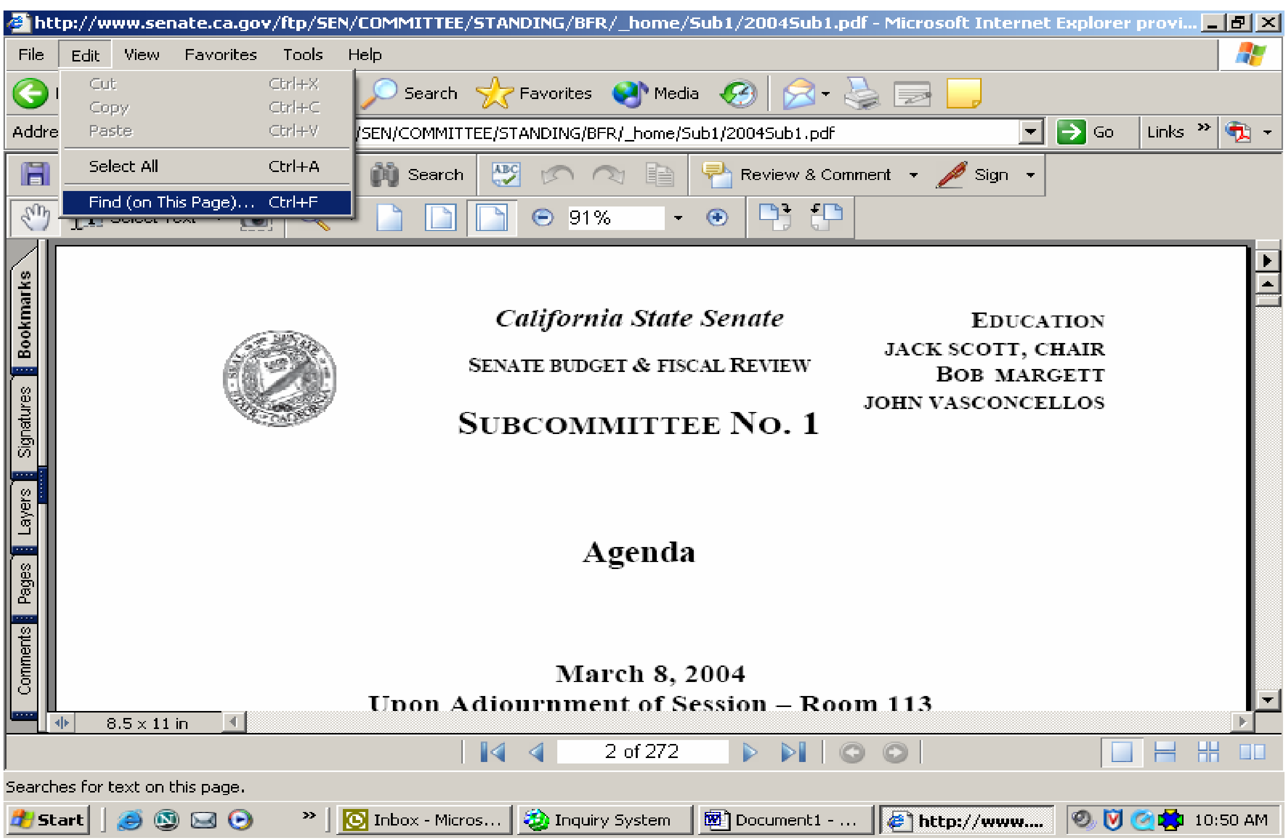

SUBCOMMITTEE NO. 4 Agenda

Senator Michael J. Rubio, Chair
Senator Noreen Evans
Senator Doug LaMalfa

Tuesday, January 25, 2011
9:00 a.m.
Room 112

Consultant: Kris Kuzmich

Item Number and Title

0840	State Controller's Office
0845	Department of Insurance
0890	Secretary of State
2320	Department of Real Estate
	State Operations Efficiencies

(See Table of Contents on page 2 for a More Specific Listing of Issues)

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AGENDA – VOTE ONLY ITEMS

(Please see summary chart on Page 3)

AGENDA – DISCUSSION / VOTE ITEMS

Issues Proposed for Vote Only:

	Issue	2011-12 Amount	Fund Source	Staff Recommendation
	State Controller's Office (0840)			
1	Women, Infants, and Children Audits	$1.8 million and 12.6 one-year limited-term positions	Reimbursements	APPROVE
2	Electronic Claim Audits	$462,000 and 4.2 two-year limited-term positions	Reimbursements	APPROVE
3	Federal Oil and Gas Audits	$314,000 and 2.0 permanent positions	Federal Funds	APPROVE
4	California Automated Travel Expense Reimbursement System	$524,000	Reimbursements	APPROVE
	Department of Insurance (0845)			
1	Paperless Workflow System Project	$2.6 million	Insurance Fund	APPROVE

Vote:

VOTE ONLY ITEMS – ISSUE DESCRIPTIONS

0840 STATE CONTROLLER'S OFFICE

For overview and budget information regarding this department, please see page 7 of this agenda.

Issue 1 – Women, Infants, and Children Audits

Governor's Budget Request. The Governor requests an increase of $1.1 million (reimbursements) in 2010-11 and 6.3 positions, and $1.8 million and 12.6 one-year limited-term positions in 2011-12, to augment existing personnel providing audit services to the California Department of Public Health (CDPH) Women, Infants, and Children (WIC) program.

Background. The SCO has been providing audit and review services on WIC providers and vendors for the CDPH for more than 20 years. Recently, the federal Department of Agriculture changed audit requirements mandating that the CDPH audit at least five percent of the WIC vendors/providers in California each year. This federal mandate will result in an additional 135 audits per year, bringing the total number of vendor compliance audits to 200 in 2010-11 and 2011-12. The CDPH is increasing the audit coverage to include national retail stores such as WalMart, Food for Less, Safeway, and WinCo. The process of auditing vendors of this size requires audit teams rather than individual auditors because of the volume of records requiring scrutiny. Therefore, the SCO audit responsibility will grow by the number of audits and in workload capacity. The SCO reports that prior WIC vendor audits disclosed a 2:1 recovery ratio for every contract dollar provided by CDPH; the SCO estimates that the $3.4 million contract amount for audit services will yield approximately $7 million in questioned costs.

Staff Comment. These audits are federally funded and required, and provided by the SCO to the CDPH on an interagency contract. This request will allow CDPH to attain the minimum level of audits mandated by the federal Department of Agriculture. The resources are requested as limited-term; should the interagency agreement between the CDPH and the SCO be extended, a future budget request would be presented.

Issue 2 – Electronic Claim Audits

Governor's Budget Request. The Governor requests 4.2 two-year limited-positions and $462,000 (reimbursements) for two years beginning in 2011-12 for processing of electronic claims.

Background. The SCO, and its Division of Audits, is responsible for auditing disbursements of State funds and to withhold payment for any claim until it has been audited in conformity with applicable laws, rules, and regulations. The Division of Audits is split into two bureaus to perform these audit functions: (1) Operations Bureau, Claim Audits – responsible for auditing manual (paper) claims; and (2) State Agency Audits Bureau, Electronic Data Processing (EDP) Audits – responsible for auditing electronic claims. In 2009-10, the EDP Audits processed approximately 9,000 claim schedules resulting in more than 36.3 million payments. Agencies contract with the SCO to implement the electronic claims process, and pay the SCO an average of $50,000 for the actual implementation costs. The EDP Audits workload has increased in recent years and is projected to continue to increase. For instance, new implementations, which average 660 hours each, have increased from 10 in 2007-08 to 16 in 2009-10, a 60 percent increase. The SCO has determined that its current resources, funded by reimbursements from client agencies, are insufficient to meet workload needs and existing staff cannot be redirected to meet the increased workload.

In 2009-10, 14.2 million in audit exceptions were found by 19.2 EDP Audits staff. Therefore, the SCO estimates that the additional 4.2 EDP Audit staff requested can produce $3.0 million in audit exceptions and potential savings to the state.

Issue 3 – Federal Oil and Gas Audits

Governor's Budget Request. The Governor requests 2.0 permanent positions and $314,000 (federal funds) to reconcile the current federal contract of $1.1 million with the federal Department of the Interior, Bureau of Ocean Energy Management, Regulation, and Enforcement.

Background. California receives a percentage of the royalty income from onshore and offshore federal leases located within its borders. Pursuant to state law, most of the money is distributed to public education and counties. For twenty years, the federal Department of the Interior has contracted with the SCO to ensure royalties are correctly reported and paid by oil and gas, geothermal resources, and solid minerals companies producing and selling energy resources from the federal leases in California. Since 2007-08, the SCO has proposed and executed a more aggressive audit approach and work plan which has increased royalty recoveries – from $2.3 million in 2007-08 to $7.8 million in 2008-09 and $3.03 million in 2009-10. The federal government has since increased the audit contract from $650,000 in 2007-08 to $1.1 million in 2010-11. This request will reconcile the current federal contract of $1.1 million with the federal Department of the Interior. The SCO reports that the resources will generate $5 million in revenue.

Issue 4 – California Automated Travel Expense Reimbursement System (CalATERS)

Governor's Budget Request. The Governor requests an increase of $524,000 (reimbursements) in 2011-12, and $702,000 in 2012-13 and ongoing, to fully support the cost of administering the CalATERS system.

Background. Prior to 2000, state employees and department accounting offices processed travel advances and expense reimbursement claims using manual, paper-based processes. In 2000, the SCO developed CalATERS, an automated system to replace the paper system and to process claims more rapidly and accurately. The system allows employees to process claims through the internet or intranet. Funding for the system came from agencies who voluntarily determined they needed a more efficient way to process travel advances. In addition to a one-time development fee, a participating agency pays a $6 transaction fee for each reimbursement claim processed through CalATERS to support the ongoing program expenditures. In 2007, legislation was passed that mandated all state agencies use the web-based CalATERS system by July 1, 2009.

Currently, approximately 105 departments use CalATERS. A few departments were granted exemptions from the statutory mandate to utilize CalATERS due to limitations of the current system, including that the system is not ADA compliant and computer incompatibility. CalATERS has since been upgraded to resolve these issues. With the increased usage of CalATERS, the upgrade to the system, and increased maintenance costs, the reimbursement authority is no longer aligned with program costs. This request will realign the reimbursement authority with programs costs; increased volumes of employee users will generate the funds to cover costs without the need to increase the fee.

0845 CALIFORNIA DEPARTMENT OF INSURANCE

For overview and budget information regarding this department, please see page 11 of this agenda.

Issue 1 – Paperless Workflow System Project

Governor's Budget Request. The Governor requests increased expenditure authority of $2.6 million (Insurance Fund) in 2011-12 to complete the final year of implementation and provide ongoing maintenance of the Paperless Workflow System Project (PWSP), which is intended to replace the current paper process with an electronic-based system

2010-11 Budget. The 2010-11 Budget provided $2.4 million (Insurance Fund) and two two-year limited-term positions to complete the second year implementation phase of the PWSP.

Staff Comment. The original implementation schedule of the PWSP was over three fiscal years (2008-09 through 2010-11). In 2008-09 and 2009-10, respectively, the Legislature approved funding for the first and second year implementation of the PWSP. However, the PWSP encountered unforeseen procurement delays in 2009-10 which pushed back the startup of the project by eight months. These delays were largely out of the control of CDI and involved problems with the Department of General Services renewing the state's Master Services Agreement. These delays have not resulted in an overall increase in the cost of the PWSP project.

0840 STATE CONTROLLER'S OFFICE

Department Overview. The State Controller is the Chief Fiscal Officer of the state. The primary functions of the State Controller's Office (SCO) are to provide sound fiscal control over both receipts and disbursements of public funds; to report periodically on the financial operations and condition of both state and local government; to make certain that money due the state is collected through fair, equitable, and effective tax administration; to provide fiscal guidance to local governments; to serve as a member of numerous policy-making state boards and commissions; and, to administer the Unclaimed Property and Property Tax Postponement Programs.

Budget Overview. The January Governor's Budget provides the SCO with 1,491 authorized positions and $218.9 million ($76.5 million GF). This is an increase of two positions and $65,000.

Issues Proposed for Discussion / Vote:

Issue 1 – 21st Century Project

Governor's Budget Request. The Governor requests $63.7 million ($34.2 million GF, $1.0 reimbursements, and $28.4 million special funds) to fund the 21st Century Project in 2011-12. The 21st Century Project will result in an integrated human resource management system that will replace the existing payroll, employment history, position management, and leave accounting systems.

2010-11 Budget. The 2010-11 budget provided 111 two-year limited-term positions and $66 million ($30 million GF, $1 million reimbursements, and $35 million special fund) for the 21st Century Project.

Background. The SCO pays approximately 249,000 employees, including state civil service, California State University and Judicial Council employees, judges, and elected officials. The 21st Century Project (Project) will replace the existing statewide human resource management systems in order to improve management processes and fulfill payroll and reporting obligations accurately and on time. The Project began in May 2004. The first deployment wave is scheduled for October 2011, comprised of 25 departments and 14,281 employees. That initial wave will be followed by three successive wave rollouts in January 2012 (50 departments and 75,841 employees), July 2012 (10 departments and 68,065 employees), and October 2012 (77 departments and 84,650 employees). The current estimated total cost (one-time and continuing) of the 21st Century Project is $303.2 million.

Staff Comment. The need to transition the State from a transaction-based system to an enterprise database system that supports the business needs of state government is clear. The key question before the Subcommittee with regard to the 21st Century Project is risk management in the deployment, including transition and training, for the new human resources system. Significant organizational change management activities will have to be undertaken to assist more than one hundred and sixty state departments to transition to the new system. Additionally, staff notes that in light of state budget cuts, a reasonable question can be raised about the capacity of departments to participate in system transition activities. In short, it is critical for the Project to have a comprehensive plan for working with departments to ensure a successful transition.

Committee Questions. Based on the above comments, the Committee may wish the Administration and SCO to provide responses to the following questions:

1. The 21st Century Project will be rolled out in waves. Which departments are included in the first wave? Why were these departments chosen? Which departments are included in the final wave, scheduled to occur in October 2012?
2. What is the current SCO deployment plan, including transition activities? Can the SCO summarize the organizational change management activities that will have to be undertaken as the 21st Century Project roll out begins this fall?

Staff Recommendation: Approve the budget request.

Vote:

Issue 2– Unclaimed Property Accounting Workload

Governor's Budget Request. The Governor requests $293,000 (Unclaimed Property Fund) for 1.0 permanent and 3.1 two-year limited-term positions in 2011-12 ($281,000 in 2012-13 and $68,000 ongoing) to support increased workload in compliance with the Unclaimed Property Law.

Background. Under current law, the SCO is responsible for safeguarding unclaimed property until it is returned to its rightful owner. As custodian for unclaimed property, the SCO must maintain accurate accounting of unclaimed property assets, and meet statutory requirements associated with such assets. In recent years, there have been legislative changes, as well as the replacement of the system used to manage the Unclaimed Property Program, which increased workload in the areas of financial accountability, corporate actions, and the collection of securities. More specifically, under Sections 1540, 1562, and 1563 of the Code of Civil Procedure (CCP), the SCO's statutory responsibilities include ensuring that claims by owners of security properties are properly paid, including the return of any unsold securities, the net proceeds of any sale, and any income or increments earned upon the property. Additionally, the SCO is statutorily required under Section 1563 CCP to sell securities that have not been claimed by the owner. Without the resources requested in this proposal, the SCO will have significant difficulty in meeting these statutory requirements.

Staff Recommendation: Approve the budget request.

Vote:

Issue 3 – Unclaimed Property Legal Costs

Governor's Budget Request. The Governor requests a two-year augmentation of $300,000 (Unclaimed Property Fund) beginning in 2011-12 to provide proper representation in legal matters associated with representing the Unclaimed Property Program in lawsuits filed against the SCO.

Background. Under current law, the SCO is responsible for safeguarding unclaimed property until it is returned to its rightful owner. Claims processed through the Unclaimed Property Program are paid, returned for insufficient information, or denied. When a claim is denied, claimants are notified of their right to commence an action against the SCO pursuant to law. When these actions are taken, the SCO has 60 days to respond. In addition to these actions by individual claimants, other actions, including class action type suits in both state and federal court have been brought against the SCO. These suits allege the program is unconstitutional, claiming the SCO has not properly administered the program and is not seeking restitution for plaintiffs. The Attorney General normally represents the SCO, but the SCO reports that the Attorney General does not have the resources to respond to all of the actions brought against the SCO. To secure proper representation, the SCO's Legal Office has contracted with outside firms to address these actions. The SCO estimates the costs of these services will be $650,000 in 2011-12 and 2012-13. The SCO is requesting the additional funds for a limited amount of time to clear the existing lawsuits for only the most complex cases; the SCO views this as more cost effective than hiring permanent staff and training them for what may eventually result in lack of workload. The SCO reports that it will be in a better position in two years to gauge the volume and complexity of lawsuits and perhaps the need for permanent staff, whether at the SCO or the Attorney General's Office.

Staff Comment. Staff notes that outstanding questions remain with regard to why the SCO would need to seek outside counsel on the unclaimed property litigation. Therefore, staff recommends that the Subcommittee hold this request open pending receipt of additional information from the SCO and Attorney General.

Staff Recommendation: Hold open pending receipt of additional information.

Vote:

Issue 4 – Airport Customer Facility Fee Audits (SB 1192)

Governor's Budget Request. The Governor requests one position and $140,000 (reimbursements) for 2010-11, and $134,000 for 2011-12, to conduct mandated independent audits of airport customer facility fees as a result of Chapter 642, Statutes of 2010 (SB 1192).

Background. Beginning in 1999, a series of bills were passed authorizing local airports to collect a customer facility fee to finance and construct a consolidated rental car facility and common-use transportation system, subject to certain conditions. The fee is now capped at $10 per customer and local airports charging the fee are required to complete an independent audit to ensure that the aggregate amount collected does not exceed the reasonable costs paid by the airport to finance, design, and construct those facilities. Further, statute requires that the independent audit be performed prior to the initial collection of, or prior to any increase in, the alternative customer facility fee and every three years thereafter.

Chapter 642, Statutes of 2010 (SB 1192) requires that the SCO review the audits and independently examine and substantiate the necessity for, and the amount of, the customer facility charge. Chapter 642 requires that the SCO's costs be reimbursed by the individual airport being audited.

Staff Comment. Chapter 642 represents new responsibility and workload for the SCO. The request before the Subcommittee is narrowly crafted in that it represents one audit position and accompanying reimbursement authority only through 2011-12. The SCO indicates that this workload is anticipated to be ongoing and may therefore request to continue this funding at a later time.

Staff Recommendation: Approve the budget request.

Vote:

0845 CALIFORNIA DEPARTMENT OF INSURANCE

Department Overview. The California Department of Insurance (CDI) regulates the California insurance market and enforces the California Insurance Code, conducting examinations and investigations of insurance companies and producers and working to ensure the financial solvency of companies so that they will meet their obligations to policyholders and claimants. CDI investigates more than 300,000 complaints annually and responds to consumer inquiries. CDI also reviews and approves insurance rates to enforce the statutory requirement that rates are not excessive or unfair. CDI also administers the conservation and liquidation of insolvent and delinquent insurance companies and fights insurance fraud in conjunction with local and state law enforcement agencies.

Budget Overview. The January Governor's Budget provides CDI with 1,338 authorized positions and $224.94 million (Insurance Fund and reimbursements). This is an increase of 71 positions and $16.4 million.

Issues Proposed for Discussion / Vote:

Issue 1 – Implementation of Federal Health Care Reform

Background. The California health insurance market is regulated by two separate agencies, the Department of Managed Health Care (DMHC) and the CDI. DMHC oversees health care service for more than 21 million insured Californians in the: individual; small employer group; large group market; Medicare Select; Medicare Supplement; and, specialized health care service plans; and regulates, 59-full service health service plans and certain preferred provider organization products operating in California. The CDI regulates all other PPO and indemnity health products provided by 98 insurers to approximately 9.3 million covered lives in the individual, small employee group, large group, and Medicare Supplement markets.

On March 23, 2010, President Obama signed the Patient Protection and Affordable Care Act (PPACA) into law, a comprehensive health reform proposal intended to expand coverage, control health care costs, and improve the health care delivery system. The PPACA makes several fundamental changes to the private health insurance market, including setting up a new competitive private health insurance market through state Exchanges beginning in 2014, and prohibitions on lifetime benefit coverage limits and rescissions of coverage. In 2010, several state statutory changes were enacted to align California law with the new federal mandates under the PPACA. These statutory changes drive 2011-12 budget requests for both the CDI and the DMHC. The following three requests pertain to increased workload at the CDI; the Subcommittee is scheduled to consider requests from the DMHC at its February 7, 2011, hearing. Generally speaking, the increased workload included in the following three requests is a result of changes in federal law; however, it is important to note that each of the bills created California-specific statutory requirements beyond the parameters of the federal PPACA mandates, as detailed in Attachment 1 to this agenda.

Issue 1.a – Health Insurance Premium Rate (SB 1163)

Governor's Budget Request. The Governor requests $1.2 million (Insurance Fund) in 2011-12, $1.1 million in 2012-13 and $100,000 ongoing, to fund 10.0 positions (8.0 two-year limited-term, 1.0 one-year limited-term, and 1.0 ongoing) to address new workload associated with the review of health insurance rate filings as a result of Chapter 661, Statutes of 2010 (SB 1163).

Background. Chapter 661 amends the law regulating health care service plans and health insurers in order to ensure that both the DMHC and CDI have the authority necessary to review the rate filings for all markets consistent with the requirements of the PPACA. The new workload consists of expanded scope and extent of the actuarial review to be undertaken by CDI, and new actuarial reporting and data trend analysis requirements.

Issue 1.b – Health Care Coverage (AB 2470)

Governor's Budget Request. The Governor requests $602,000 (Insurance Fund) in 2011-12, and $602,000 in 2012-13, to fund 6.0 Staff Counsel positions on a two-year limited-term basis to support the additional rate filings and new cancellation and non-renewal appeal process as a result of Chapter 658, Statutes of 2010 (AB 2470).

Background. Chapter 658: (1) imposes new requirements on an insurers' ability to cancel, rescind, and non-renew health insurance policies; (2) creates a system whereby the Commissioner will review the propriety of cancellations, rescissions, and non-renewals where the insured has complained with the insurer being entitled to a hearing; and (3) provides a mechanism for a policyholder, certificate holder, or other insured who alleges that a policy or coverage has been or will be cancelled, rescinded, or not renewed in violation of law to require a review by the Commissioner. This request will provide the resources to implement new workload required by Chapter 658 regarding industry cancellation, rescission, and non-renewal practices and to provide policyholders with the required review mechanisms.

Issue 1.c – Health Benefit Exchange (SB 900 and AB 1602)

Governor's Budget Request. The Governor requests $107,000 (Insurance Fund) in 2011-12, and $100,000 in 2012-13, to fund one staff counsel position on a two-year limited-term basis to support the additional policy form review activities required as a result of the implementation of the California Health Benefits Exchange established by Chapters 659 and 655, Statutes of 2010 (SB 900 and AB 1602, respectively).

Background. Chapter 659: (1) creates the California Health Benefits Exchange (Exchange), an independent public entity, and delineates its composition and the operation of the executive board of the Exchange, and (2) requires a review of the federal Health and Human Service internet portal prior to January 1, 2015, to determine whether it provides sufficient information to facilitate fair and affirmative marketing of all individual and small employer health insurance. If the review determines the federal portal to be inadequate, Chapter 659 requires the establishment and maintenance of an electronic clearinghouse.

Chapter 655 enacts the California Patient Protection and Affordable Care Act, and provides the Exchange with operational authority, as well as authority to implement the Exchange and navigator provisions of the PPACA by 2014.

Staff Comment. With the exception of one the ongoing position included in request Health Insurance Premium Rate (SB 1163), these three budget requests represent limited-term resources. This is appropriate, as the full extent of the workload related to PPACA and changes in state law is not fully known. By approving these requests as limited-term, the Legislature can review the workload and ensure the appropriate budget resources are provided in future budget cycles. Additionally, staff notes that approving the resources as limited-term will also allow time for study and analysis of whether or not California wants to continue to have two departments, DMHC and CDI, regulating the insurance market.

Staff Recommendation: Approve the budget requests; with regard to request Health Insurance Benefit Premium (SB 1163), staff recommends that the position proposed as ongoing instead be approved as two-year limited-term.

Vote:

Issue 2 – Department of Insurance Workload Resource Augmentation

Governor's Budget Request. The Governor requests an increase of $7.9 million (Insurance Fund) in 2011-12, and $7.0 million ongoing, to fund 54.0 positions to address increased workload while continuing to meet statutory mandates.

Background. The CDI reports that its workload has increased in recent years without a commensurate increase in staffing resources. Further, in 2009-10 the CDI budget was permanently reduced by $17.4 million through a line-item veto action. As a result of this reduction, CDI reports that backlogs are increasing throughout the department, including in the Rate Regulation Branch, which has a backlog of 1,080 files; the Field Examination Division, which has examined only two title companies compared to 19 in 2008; and, the Consumer Services Division, where complaints have increased 11 percent and complex health insurance complaints have increased 118 percent. CDI indicates that the resources in this request will not eliminate the backlog throughout the department. Rather, the resources will allow the Department to address the backlog and then remain even with workload going forward. CDI proposes to apportion the resources in this request as follows:

Division	2010-11 Positions	2011-12 New Positions	2011-12 Add'l Funding
Rate Regulation	88.0	2.0	268,000
Financial Surveillance	161.0	5.0	774,000
Executive	26.0	2.0	156,000
Consumer Services & Market Conduct	151.0	10.0	1,175,000
Investigation	92.0	6.0	1,019,000
Fraud	289.0	14.0	2,931,000
Legal	125.0	14.0	1,492,000
Administration & Licensing	280.0	1.0	121,000
		54.0	**$7,936,000**

Staff Comment. Staff notes that the LAO is currently undertaking a workload analysis of this request and is therefore withholding any recommendation to the Legislature until that analysis is complete. The Subcommittee may wish to wait to consider this request until after the LAO analysis is complete.

Staff Recommendation: Hold open pending receipt of the LAO's workload analysis.

Vote:

0890 SECRETARY OF STATE

Department Overview. The Secretary of State (SOS), a constitutionally established office, is the chief election officer of the state and is responsible for the administration and enforcement of election laws. The SOS is also responsible for the administration and enforcement of laws pertaining to filing documents associated with corporations, limited partnerships, and perfecting security agreements. In addition, the SOS is responsible for the appointment of notaries public, enforcement of notary laws, and preservation of documents and records having historical significance. All documents filed are a matter of public record and of historical importance. They are available through prescribed procedures for public review and to certify authenticity.

Budget Overview. The January Governor's Budget provides the SOS with 505 authorized positions and $161.5 million ($31.1 million GF). This is a decrease of no positions and $10.9 million.

Issues Proposed for Discussion / Vote:

Issue 1 – Help America Vote Act Amended Spending Plan

Governor's Budget Request. The Governor requests expenditure authority of $70 million (federal funds) in 2011-12 to continue implementation of the statewide mandates of the federal Help America Vote Act of 2002 (HAVA).

2010-11 Budget. The 2010-11 budget provided $4.2 million (federal funds) to continue implementation of HAVA-related state mandates, including assistance for individuals with disabilities, voting systems testing/certification, voter education, performance measures, and administration.

Background. Generally speaking, the federal HAVA requires state and localities to meet uniform and nondiscriminatory election technology and administration requirements applicable to federal elections. Federal HAVA funding was originally received by the state in 2003, and a spending plan was required by the Legislature in 2004 and approved in April 2005. The SOS revises the HAVA spending plan annually to accurately reflect actual spending, and propose changes for future spending based on new funding and changes in expenditures.

Of the $70 million (federal funds) included in this request, $66.9 million is proposed as local assistance to counties and $3.2 million is for state operations. Of the $66.9 million in local assistance, $65.9 million is for voting system upgrades and $1.0 million is for elections assistance for individuals with disabilities. The voting system upgrades are required under HAVA to ensure an accessible, voter-verifiable paper audit trail. The state operations funding will be utilized for the continued administration of statewide modernization and replacement of voting equipment; education and training programs for elections officials and poll workers; and, development and dissemination of voting information to increase voter participation and confidence.

Staff Comment. This request does not include funding for the VoteCal project, which is the HAVA-required uniform, centralized, interactive computerized voter registration database that is defined, maintained, and administered at the state level. That request is discussed as Issue 2 below.

Staff Recommendation: Approve the budget request.

Vote:

Issue 2 – Help America Vote Act, VoteCal

Governor's Budget Request. The Governor requests expenditure authority of $11.6 million (federal funds) in 2011-12 to continue implementation of VoteCal, the federal Help America Vote Act (HAVA)-required and funded uniform, centralized, interactive computerized voter registration database that is defined, maintained, and administered at the state level.

2010-11 Budget. The 2010-11 budget included $23 million (federal funds) to continue implementation of VoteCal.

Background. Under federal HAVA requirements, VoteCal must coordinate electronically with systems similar to the one used by the Department of Motor Vehicles, the Department of Health Care Services, and the Department of Corrections and Rehabilitation for identification and list maintenance purposes. VoteCal must also provide a functional interface for counties. California reached an interim solution to satisfy the requirements of HAVA, but must achieve a long-term solution per an agreement with the U.S. Department of Justice. VoteCal is that solution.

Staff Comment. The 2011-12 request is consistent with previous updates and continues to appropriately administer the HAVA-required VoteCal system. Staff notes, however, that due to the fact that the initial system integration (SI) vendor failed to provide the contractually required performance bond, which required the SOS to terminate the contract in May 2010, the SOS now estimates that the VoteCal project will be extended until June 2014. This is 1.25 years beyond the previously projected and approved February 2012 completion date. The greatest impact on the schedule is the 16 months it will take to sign a contract with a new SI vendor. Approximately $6.6 million of the resources included in this request are for payment to the SI vendor in 2011-12. Due to the re-procurement delay, it is highly unlikely that these funds will be fully expended in 2011-12, but staff notes that the allocation level is within the parameters of the approved project documents. Further, it would be difficult at best to estimate the 2011-12 SI vendor costs and, in any case, the unused federal funds will roll forward to 2012-13 and be reflected in a budget request for that fiscal year.

Staff Recommendation: Approve the budget request.

Vote:

2320 DEPARTMENT OF REAL ESTATE

Department Overview. A primary objective of the Department of Real Estate (DRE) is to protect the public in real estate transactions and provide licensing, regulatory, and subdivision services to the real estate industries. The DRE is entirely special funded (Real Estate Fund) and derives its revenues from examination, license, and subdivision fees. The core functions of the DRE are to administer license examinations, issue real estate licenses, regulate real estate licensees, and qualify subdivision offerings.

Budget Overview. The January Governor's Budget provides DRE with 381 authorized positions and $46.0 million (RE Fund and reimbursements). This is an increase of two positions and $1.5 million.

Issue Proposed for Discussion / Vote:

Issue 1 – SB 36 Mortgage Loan Originator Licensure (SAFE Act)

Governor's Budget Request. The Governor requests $216,000 (Real Estate Fund) and two positions for continued implementation of the federally mandated Secure and Fair Enforcement Licensing Act of 2008 (SAFE Act) which requires states to implement a new licensing program for mortgage loan originators (MLOs).

2010-11 Budget. The 2010-11 budget included $2.8 million (Real Estate Fund) and 27 positions to begin implementation of the SAFE Act.

Background. The federally mandated SAFE Act requires all states to license and register their MLOs through a nationwide registry called the National Mortgage Licensing System (NMLS). Chapter 160, Statutes of 2009 (SB 36), brought California into compliance with the SAFE Act by requiring those engaging in MLO activities to obtain a license from the Department of Corporations or, if a real estate licensee, obtain a license endorsement from the DRE.

The SAFE Act requirements are similar to, but somewhat different from, the requirements for licensure under California's Real Estate Law. At this point in the SAFE Act implementation process, the main drivers of new licensing and enforcement workload for the DRE will be the MLO notification process and the annual Business Activities Report requirement for all MLO brokers. The amount of new workload will be driven by the number of NMLS registrants; as of December 31, 2010, an estimated 37,373 individuals and over 6,133 real estate companies who perform MLO activities registered on NMLS. The DRE expects additional late registration activity, as licensees become aware of the NMLS registration requirement.

DRE reports that it will be able to comply with existing SB 36 requirements with the resources in this request. However, because DRE is only now compiling final workload data based on the total number of licensees who registered on the NMLS, and the complexity of licensing and enforcement is better known, DRE indicates that this request is a precursor to an additional request for positions, technology enhancements, and budget authority in a Spring 2011 Budget Letter.

Staff Comment. In approving SB 36, the Legislature approached SAFE Act compliance in a narrow sense by requiring a new endorsement on existing real estate licenses. Licensees pay a $300 fee for that endorsement. Staff notes that while this approach has resulted in the least disruption to existing systems and minimized compliance costs to both the state and licensees, the SAFE Act has represented, and will continue to represent, new workload for DRE.

However, as noted above, DRE indicates that a Spring 2011 Budget Letter is planned to request budget authority and positions beyond that contained in this request. Additionally, DRE faces a facility issue which remains unresolved from 2009-10. Last year, this Subcommittee specifically requested that DRE present a formal request during the 2011-12 budget process to ensure that DRE did not absorb the costs of relocating and consolidating its Sacramento facilities within its existing budget, an action that could result in decreased enforcement and consumer protection activities. DRE indicates that it plans to present a separate Spring 2011 Budget Letter for the Sacramento headquarters move costs. Finally, staff notes that the Senate Business and Professions Committee is holding an oversight hearing on February 28, 2011, focused on DRE enforcement and consumer protection issues. Given these factors, staff recommends that this request be denied without prejudice and instead wait to consider this request in the context of the Spring 2011 requests from DRE, as well as the findings from the Senate Business and Professions Committee oversight hearing.

Staff Recommendation: Deny the budget request without prejudice; consider during the Spring 2011 budget process.

Vote:

STATE OPERATIONS EFFICIENCIES

Issue Proposed for Discussion Only

Issue 1 – State Operations Efficiencies

Governor's Budget Request. The January Governor's Budget includes $363 million ($200 million GF) in savings associated with identification of efficiencies in state operations, including identification of agencies, departments, and programs that can be reorganized to eliminate duplication and unnecessary functions; review of state peace officer and safety classifications; and reductions in other areas like contracting, fleet operations, and cell phone use.

Background. The Governor's January budget begins what is described as an ongoing effort to make state government more effective and efficient by reducing costs, improving timelines, and reducing overlapping responsibilities. In 2010-11, the Governor has taken steps to accomplish these goals by taking the following actions: (1) eliminating the Office of the Secretary of Education; (2) eliminating the American Recovery and Reinvestment Act Inspector General and transferring ongoing work to other established oversight entities, including the Bureau of State Audits and State Controller's Office; and (3) reducing the Governor's Office budget by 25 percent. Additional 2010-11 savings were achieved by spending only $120,000 of the $770,000 budgeted for transition costs.

Separately, the Governor has directed agency secretaries and department directors to immediately review their operational costs and identify options to generate savings. Two immediate areas of focus are use of cell phones by state employees and the number of state vehicles:

1. With regard to cell phones, the state currently pays for approximately 96,000 cell phones, one for over 40 percent of all state employees. Via an Executive Order issued on January 11, 2011, the Governor ordered all agency secretaries and department directors to: (1) document and review all authorized cell phone and smart phone procurement and related phone, data, internet and other usage plans for and by their employees and (2) identify and implement by June 1, 2011, cuts sufficient to meet or exceed a 50 percent decrease in the number of cell phones and smart phones for which the state is currently responsible and achieve at least $20 million (all funds) in savings.

2. With regard to the state fleet, which totals 13,600 vehicles (not including some 12,000 vehicles that are used for public safety), the Administration indicates it will reduce the number of vehicles the state maintains by requiring each vehicle's purpose and necessity to be rejustified. Only vehicles necessary for critical state functions will be retained, and only when retaining such vehicles is cost effective.

The mechanism to achieve these savings is Control Section 3.91, which requires that the Director of Finance allocate the reductions necessary to each item of appropriation in the budget to accomplish the required savings.

Staff Comment. The overarching goal of seeking greater efficiency and effectiveness in state operations is worthwhile. By beginning with cell/smart phones and fleet management, the Administration has identified two areas which will likely bear some fruit. Staff understands that the Administration has a "living list" of additional areas of exploration, including micro items such as toll-free telephone lines and macro items such as executive branch reorganization plans. At some point, this list will have to be narrowed, or triaged, to permit the focused work to occur to build to the point where real savings are achieved in 2011-12.

Committee Questions. Based on the above comments, the Committee may wish the Administration to provide responses to the following questions:

1. What other specific areas is the Administration currently considering for increased efficiency and effectiveness?
2. What is the timeframe for this process?
3. How can the Legislature be of assistance to the Administration in this process?

Staff Recommendation: No action; information item only.

ATTACHMENT 1

Differences Between the Federal Affordable Care Act and 2010 California Health Reform Legislation That Have a Workload Impact on the Department of Insurance

	Federal	State
SB 1163: Rate Review		
Individual/Small Group rate filings	Only rate increases in excess of 10% must be filed. (45 CFR 154.200), does not apply to grandfathered plans. (45 CFR 154.103(b))	**All** individual and small group rates must be filed. (IC 10181.3(a))
Data required in filing	18 elements (45 CFR 154.210(e),(g))	25 elements (e.g., IC 10181.3(b))
Examples of differences in data requirements:		
Trend projections	Utilization, service/unit co st (45 CFR 154.215(e)(2))	Utilization, price inflation, fees and risk, broken down into 7 aggregate benefit categories (e.g., IC 10181.3(b)(19))
Cost containment/quality improvement data	Not required	Required (e.g.: IC 10181.2(b))
Actuarial certification by outside actuary	Not required	Required (IC 10181.6)
Criteria re: independence of outside actuary	Not required	Required. CDI will have to evaluate.
Filing must be actuarially sound	Not required	Required (IC 10181.6). CDI will have to evaluate.
Aggregate Reporting Requirements	Medical loss ratio data (45 CFR 158.110-170)	9 data elements, not including medical loss ratio (IC 10181.3(c), 10181.4(c))
Carrier-provider contract rates	Not discussed	Received by CDI, must be segregated, kept confidential. (IC 10181.7(b))
Actions Required of CDI	Receive filings (PPACA 2794), provide information to HHS, including premium trends (PPACA 2794(b),(c))	CDI must review filings to detect violations (IC 10181.11), CDI must make findings regarding rate justifications and post on website (IC 10181.11(f)),CDI must make all submitted information public (IC 10181.7(a)), CDI must make quarterly reports to Legislature (IC 10181.11(d)).

AB 2470: Cancellation/Nonrenewal/ Rescission		
Applicable to non-renewal?	No. Applies only to rescission. (PPACA 2712)	Applies to rescission, cancellation, non-renewal (IC 10273.4(b)). Expanded scope means expanded CDI policy form review beyond federal requirements.
CDI review and hearing process for cancellations, rescission, non-renewal	Not required in federal law.	Requires CDI to establish a process to review complaints to determine adequacy, reinstate coverage, and a hearing process for carrier appeals.
SB 900/AB 1602: Exchange		
Review of Exchange policy forms by CDI	Required if federal government operates exchange	Required if state operates exchange
Include California health mandates	California mandates not required.	State has option to include California mandates in Exchange policies, which increases complexity of policy review.
Plans offered	Policies offered in exchange need not all be offered outside exchange.	All policies offered inside exchange must also be offered outside exchange (IC 10112.3 (c)). Increases CDI review load.
Federal Internet Portal	Maintained by HHS	CDI & DMHC must review HHS site to determine if meets requirement for affirmative marketing, especially outside exchange. If inadequate, CDI & DMHC must establish clearinghouse.
Catastrophic coverage	Carriers that do not participate in Exchange may sell catastrophic coverage	Carriers that do not participate in exchange cannot sell catastrophic coverage (IC 10112.3(d)). Adds additional element to CDI market conduct examinations.

Bruce Hinze, January 22, 2011

Senate Budget and Fiscal Review—Mark Leno, Chair

SUBCOMMITTEE NO. 4 Agenda

Senator Michael J. Rubio, Chair
Senator Noreen Evans
Senator Doug LaMalfa

Tuesday, January 25, 2011
9:00 a.m.
Room 112

Consultant: Kris Kuzmich

OUTCOMES

Item Number and Title

0840	State Controller's Office
0845	Department of Insurance
0890	Secretary of State
2320	Department of Real Estate
	State Operations Efficiencies

(See Table of Contents on page 2 for a More Specific Listing of Issues)

Pursuant to the Americans with Disabilities Act, individuals who, because of a disability, need special assistance to attend or participate in a Senate Committee hearing, or in connection with other Senate services, may request assistance at the Senate Rules Committee, 1020 N Street, Suite 255 or by calling 916-324-9335. Requests should be made one week in advance whenever possible.

AGENDA – VOTE ONLY ITEMS

(Please see summary chart on Page 3)

AGENDA – DISCUSSION / VOTE ITEMS

Issues Proposed for Vote Only:

	Issue	2011-12 Amount	Fund Source	Staff Recommendation
	State Controller's Office (0840)			
1	Women, Infants, and Children Audits	$1.8 million and 12.6 one-year limited-term positions	Reimbursements	APPROVE
2	Electronic Claim Audits	$462,000 and 4.2 two-year limited-term positions	Reimbursements	APPROVE
3	Federal Oil and Gas Audits	$314,000 and 2.0 permanent positions	Federal Funds	APPROVE
4	California Automated Travel Expense Reimbursement System	$524,000	Reimbursements	APPROVE
	Department of Insurance (0845)			
1	Paperless Workflow System Project	$2.6 million	Insurance Fund	APPROVE

Vote: All proposed vote only issues approved 3-0.

VOTE ONLY ITEMS – ISSUE DESCRIPTIONS

0840 STATE CONTROLLER'S OFFICE

For overview and budget information regarding this department, please see page 7 of this agenda.

Issue 1 – Women, Infants, and Children Audits

Governor's Budget Request. The Governor requests an increase of $1.1 million (reimbursements) in 2010-11 and 6.3 positions, and $1.8 million and 12.6 one-year limited-term positions in 2011-12, to augment existing personnel providing audit services to the California Department of Public Health (CDPH) Women, Infants, and Children (WIC) program.

Background. The SCO has been providing audit and review services on WIC providers and vendors for the CDPH for more than 20 years. Recently, the federal Department of Agriculture changed audit requirements mandating that the CDPH audit at least five percent of the WIC vendors/providers in California each year. This federal mandate will result in an additional 135 audits per year, bringing the total number of vendor compliance audits to 200 in 2010-11 and 2011-12. The CDPH is increasing the audit coverage to include national retail stores such as WalMart, Food for Less, Safeway, and WinCo. The process of auditing vendors of this size requires audit teams rather than individual auditors because of the volume of records requiring scrutiny. Therefore, the SCO audit responsibility will grow by the number of audits and in workload capacity. The SCO reports that prior WIC vendor audits disclosed a 2:1 recovery ratio for every contract dollar provided by CDPH; the SCO estimates that the $3.4 million contract amount for audit services will yield approximately $7 million in questioned costs.

Staff Comment. These audits are federally funded and required, and provided by the SCO to the CDPH on an interagency contract. This request will allow CDPH to attain the minimum level of audits mandated by the federal Department of Agriculture. The resources are requested as limited-term; should the interagency agreement between the CDPH and the SCO be extended, a future budget request would be presented.

Issue 2 – Electronic Claim Audits

Governor's Budget Request. The Governor requests 4.2 two-year limited-positions and $462,000 (reimbursements) for two years beginning in 2011-12 for processing of electronic claims.

Background. The SCO, and its Division of Audits, is responsible for auditing disbursements of State funds and to withhold payment for any claim until it has been audited in conformity with applicable laws, rules, and regulations. The Division of Audits is split into two bureaus to perform these audit functions: (1) Operations Bureau, Claim Audits – responsible for auditing manual (paper) claims; and (2) State Agency Audits Bureau, Electronic Data Processing (EDP) Audits – responsible for auditing electronic claims. In 2009-10, the EDP Audits processed approximately 9,000 claim schedules resulting in more than 36.3 million payments. Agencies contract with the SCO to implement the electronic claims process, and pay the SCO an average of $50,000 for the actual implementation costs. The EDP Audits workload has increased in recent years and is projected to continue to increase. For instance, new implementations, which average 660 hours each, have increased from 10 in 2007-08 to 16 in 2009-10, a 60 percent increase. The SCO has determined that its current resources, funded by reimbursements from client agencies, are insufficient to meet workload needs and existing staff cannot be redirected to meet the increased workload.

In 2009-10, 14.2 million in audit exceptions were found by 19.2 EDP Audits staff. Therefore, the SCO estimates that the additional 4.2 EDP Audit staff requested can produce $3.0 million in audit exceptions and potential savings to the state.

Issue 3 – Federal Oil and Gas Audits

Governor's Budget Request. The Governor requests 2.0 permanent positions and $314,000 (federal funds) to reconcile the current federal contract of $1.1 million with the federal Department of the Interior, Bureau of Ocean Energy Management, Regulation, and Enforcement.

Background. California receives a percentage of the royalty income from onshore and offshore federal leases located within its borders. Pursuant to state law, most of the money is distributed to public education and counties. For twenty years, the federal Department of the Interior has contracted with the SCO to ensure royalties are correctly reported and paid by oil and gas, geothermal resources, and solid minerals companies producing and selling energy resources from the federal leases in California. Since 2007-08, the SCO has proposed and executed a more aggressive audit approach and work plan which has increased royalty recoveries – from $2.3 million in 2007-08 to $7.8 million in 2008-09 and $3.03 million in 2009-10. The federal government has since increased the audit contract from $650,000 in 2007-08 to $1.1 million in 2010-11. This request will reconcile the current federal contract of $1.1 million with the federal Department of the Interior. The SCO reports that the resources will generate $5 million in revenue.

Issue 4 – California Automated Travel Expense Reimbursement System (CalATERS)

Governor's Budget Request. The Governor requests an increase of $524,000 (reimbursements) in 2011-12, and $702,000 in 2012-13 and ongoing, to fully support the cost of administering the CalATERS system.

Background. Prior to 2000, state employees and department accounting offices processed travel advances and expense reimbursement claims using manual, paper-based processes. In 2000, the SCO developed CalATERS, an automated system to replace the paper system and to process claims more rapidly and accurately. The system allows employees to process claims through the internet or intranet. Funding for the system came from agencies who voluntarily determined they needed a more efficient way to process travel advances. In addition to a one-time development fee, a participating agency pays a $6 transaction fee for each reimbursement claim processed through CalATERS to support the ongoing program expenditures. In 2007, legislation was passed that mandated all state agencies use the web-based CalATERS system by July 1, 2009.

Currently, approximately 105 departments use CalATERS. A few departments were granted exemptions from the statutory mandate to utilize CalATERS due to limitations of the current system, including that the system is not ADA compliant and computer incompatibility. CalATERS has since been upgraded to resolve these issues. With the increased usage of CalATERS, the upgrade to the system, and increased maintenance costs, the reimbursement authority is no longer aligned with program costs. This request will realign the reimbursement authority with programs costs; increased volumes of employee users will generate the funds to cover costs without the need to increase the fee.

0845 CALIFORNIA DEPARTMENT OF INSURANCE

For overview and budget information regarding this department, please see page 11 of this agenda.

Issue 1 – Paperless Workflow System Project

Governor's Budget Request. The Governor requests increased expenditure authority of $2.6 million (Insurance Fund) in 2011-12 to complete the final year of implementation and provide ongoing maintenance of the Paperless Workflow System Project (PWSP), which is intended to replace the current paper process with an electronic-based system

2010-11 Budget. The 2010-11 Budget provided $2.4 million (Insurance Fund) and two two-year limited-term positions to complete the second year implementation phase of the PWSP.

Staff Comment. The original implementation schedule of the PWSP was over three fiscal years (2008-09 through 2010-11). In 2008-09 and 2009-10, respectively, the Legislature approved funding for the first and second year implementation of the PWSP. However, the PWSP encountered unforeseen procurement delays in 2009-10 which pushed back the startup of the project by eight months. These delays were largely out of the control of CDI and involved problems with the Department of General Services renewing the state's Master Services Agreement. These delays have not resulted in an overall increase in the cost of the PWSP project.

0840 STATE CONTROLLER'S OFFICE

Department Overview. The State Controller is the Chief Fiscal Officer of the state. The primary functions of the State Controller's Office (SCO) are to provide sound fiscal control over both receipts and disbursements of public funds; to report periodically on the financial operations and condition of both state and local government; to make certain that money due the state is collected through fair, equitable, and effective tax administration; to provide fiscal guidance to local governments; to serve as a member of numerous policy-making state boards and commissions; and, to administer the Unclaimed Property and Property Tax Postponement Programs.

Budget Overview. The January Governor's Budget provides the SCO with 1,491 authorized positions and $218.9 million ($76.5 million GF). This is an increase of two positions and $65,000.

Issues Proposed for Discussion / Vote:

Issue 1 – 21st Century Project

Governor's Budget Request. The Governor requests $63.7 million ($34.2 million GF, $1.0 reimbursements, and $28.4 million special funds) to fund the 21st Century Project in 2011-12. The 21st Century Project will result in an integrated human resource management system that will replace the existing payroll, employment history, position management, and leave accounting systems.

2010-11 Budget. The 2010-11 budget provided 111 two-year limited-term positions and $66 million ($30 million GF, $1 million reimbursements, and $35 million special fund) for the 21st Century Project.

Background. The SCO pays approximately 249,000 employees, including state civil service, California State University and Judicial Council employees, judges, and elected officials. The 21st Century Project (Project) will replace the existing statewide human resource management systems in order to improve management processes and fulfill payroll and reporting obligations accurately and on time. The Project began in May 2004. The first deployment wave is scheduled for October 2011, comprised of 25 departments and 14,281 employees. That initial wave will be followed by three successive wave rollouts in January 2012 (50 departments and 75,841 employees), July 2012 (10 departments and 68,065 employees), and October 2012 (77 departments and 84,650 employees). The current estimated total cost (one-time and continuing) of the 21st Century Project is $303.2 million.

Staff Comment. The need to transition the State from a transaction-based system to an enterprise database system that supports the business needs of state government is clear. The key question before the Subcommittee with regard to the 21st Century Project is risk management in the deployment, including transition and training, for the new human resources system. Significant organizational change management activities will have to be undertaken to assist more than one hundred and sixty state departments to transition to the new system. Additionally, staff notes that in light of state budget cuts, a reasonable question can be raised about the capacity of departments to participate in system transition activities. In short, it is critical for the Project to have a comprehensive plan for working with departments to ensure a successful transition.

Committee Questions. Based on the above comments, the Committee may wish the Administration and SCO to provide responses to the following questions:

1. The 21st Century Project will be rolled out in waves. Which departments are included in the first wave? Why were these departments chosen? Which departments are included in the final wave, scheduled to occur in October 2012?
2. What is the current SCO deployment plan, including transition activities? Can the SCO summarize the organizational change management activities that will have to be undertaken as the 21st Century Project roll out begins this fall?

Staff Recommendation: Approve the budget request.

Vote: Budget request approved 3-0.

Issue 2– Unclaimed Property Accounting Workload

Governor's Budget Request. The Governor requests $293,000 (Unclaimed Property Fund) for 1.0 permanent and 3.1 two-year limited-term positions in 2011-12 ($281,000 in 2012-13 and $68,000 ongoing) to support increased workload in compliance with the Unclaimed Property Law.

Background. Under current law, the SCO is responsible for safeguarding unclaimed property until it is returned to its rightful owner. As custodian for unclaimed property, the SCO must maintain accurate accounting of unclaimed property assets, and meet statutory requirements associated with such assets. In recent years, there have been legislative changes, as well as the replacement of the system used to manage the Unclaimed Property Program, which increased workload in the areas of financial accountability, corporate actions, and the collection of securities. More specifically, under Sections 1540, 1562, and 1563 of the Code of Civil Procedure (CCP), the SCO's statutory responsibilities include ensuring that claims by owners of security properties are properly paid, including the return of any unsold securities, the net proceeds of any sale, and any income or increments earned upon the property. Additionally, the SCO is statutorily required under Section 1563 CCP to sell securities that have not been claimed by the owner. Without the resources requested in this proposal, the SCO will have significant difficulty in meeting these statutory requirements.

Staff Recommendation: Approve the budget request.

Vote: Budget request approved 2-1; Senator La Malfa voting no.

Issue 3 – Unclaimed Property Legal Costs

Governor's Budget Request. The Governor requests a two-year augmentation of $300,000 (Unclaimed Property Fund) beginning in 2011-12 to provide proper representation in legal matters associated with representing the Unclaimed Property Program in lawsuits filed against the SCO.

Background. Under current law, the SCO is responsible for safeguarding unclaimed property until it is returned to its rightful owner. Claims processed through the Unclaimed Property Program are paid, returned for insufficient information, or denied. When a claim is denied, claimants are notified of their right to commence an action against the SCO pursuant to law. When these actions are taken, the SCO has 60 days to respond. In addition to these actions by individual claimants, other actions, including class action type suits in both state and federal court have been brought against the SCO. These suits allege the program is unconstitutional, claiming the SCO has not properly administered the program and is not seeking restitution for plaintiffs. The Attorney General normally represents the SCO, but the SCO reports that the Attorney General does not have the resources to respond to all of the actions brought against the SCO. To secure proper representation, the SCO's Legal Office has contracted with outside firms to address these actions. The SCO estimates the costs of these services will be $650,000 in 2011-12 and 2012-13. The SCO is requesting the additional funds for a limited amount of time to clear the existing lawsuits for only the most complex cases; the SCO views this as more cost effective than hiring permanent staff and training them for what may eventually result in lack of workload. The SCO reports that it will be in a better position in two years to gauge the volume and complexity of lawsuits and perhaps the need for permanent staff, whether at the SCO or the Attorney General's Office.

Staff Comment. Staff notes that outstanding questions remain with regard to why the SCO would need to seek outside counsel on the unclaimed property litigation. Therefore, staff recommends that the Subcommittee hold this request open pending receipt of additional information from the SCO and Attorney General.

Staff Recommendation: Hold open pending receipt of additional information.

Vote: Budget request held open, 3-0 vote.

Issue 4 – Airport Customer Facility Fee Audits (SB 1192)

Governor's Budget Request. The Governor requests one position and $140,000 (reimbursements) for 2010-11, and $134,000 for 2011-12, to conduct mandated independent audits of airport customer facility fees as a result of Chapter 642, Statutes of 2010 (SB 1192).

Background. Beginning in 1999, a series of bills were passed authorizing local airports to collect a customer facility fee to finance and construct a consolidated rental car facility and common-use transportation system, subject to certain conditions. The fee is now capped at $10 per customer and local airports charging the fee are required to complete an independent audit to ensure that the aggregate amount collected does not exceed the reasonable costs paid by the airport to finance, design, and construct those facilities. Further, statute requires that the independent audit be performed prior to the initial collection of, or prior to any increase in, the alternative customer facility fee and every three years thereafter.

Chapter 642, Statutes of 2010 (SB 1192) requires that the SCO review the audits and independently examine and substantiate the necessity for, and the amount of, the customer facility charge. Chapter 642 requires that the SCO's costs be reimbursed by the individual airport being audited.

Staff Comment. Chapter 642 represents new responsibility and workload for the SCO. The request before the Subcommittee is narrowly crafted in that it represents one audit position and accompanying reimbursement authority only through 2011-12. The SCO indicates that this workload is anticipated to be ongoing and may therefore request to continue this funding at a later time.

Staff Recommendation: Approve the budget request.

Vote: Budget request approved 2-1; Senator La Malfa voting no.

0845 CALIFORNIA DEPARTMENT OF INSURANCE

Department Overview. The California Department of Insurance (CDI) regulates the California insurance market and enforces the California Insurance Code, conducting examinations and investigations of insurance companies and producers and working to ensure the financial solvency of companies so that they will meet their obligations to policyholders and claimants. CDI investigates more than 300,000 complaints annually and responds to consumer inquiries. CDI also reviews and approves insurance rates to enforce the statutory requirement that rates are not excessive or unfair. CDI also administers the conservation and liquidation of insolvent and delinquent insurance companies and fights insurance fraud in conjunction with local and state law enforcement agencies.

Budget Overview. The January Governor's Budget provides CDI with 1,338 authorized positions and $224.94 million (Insurance Fund and reimbursements). This is an increase of 71 positions and $16.4 million.

Issues Proposed for Discussion / Vote:

Issue 1 – Implementation of Federal Health Care Reform

Background. The California health insurance market is regulated by two separate agencies, the Department of Managed Health Care (DMHC) and the CDI. DMHC oversees health care service for more than 21 million insured Californians in the: individual; small employer group; large group market; Medicare Select; Medicare Supplement; and, specialized health care service plans; and regulates, 59-full service health service plans and certain preferred provider organization products operating in California. The CDI regulates all other PPO and indemnity health products provided by 98 insurers to approximately 9.3 million covered lives in the individual, small employee group, large group, and Medicare Supplement markets.

On March 23, 2010, President Obama signed the Patient Protection and Affordable Care Act (PPACA) into law, a comprehensive health reform proposal intended to expand coverage, control health care costs, and improve the health care delivery system. The PPACA makes several fundamental changes to the private health insurance market, including setting up a new competitive private health insurance market through state Exchanges beginning in 2014, and prohibitions on lifetime benefit coverage limits and rescissions of coverage. In 2010, several state statutory changes were enacted to align California law with the new federal mandates under the PPACA. These statutory changes drive 2011-12 budget requests for both the CDI and the DMHC. The following three requests pertain to increased workload at the CDI; the Subcommittee is scheduled to consider requests from the DMHC at its February 7, 2011, hearing. Generally speaking, the increased workload included in the following three requests is a result of changes in federal law; however, it is important to note that each of the bills created California-specific statutory requirements beyond the parameters of the federal PPACA mandates, as detailed in Attachment 1 to this agenda.

Issue 1.a – Health Insurance Premium Rate (SB 1163)

Governor's Budget Request. The Governor requests $1.2 million (Insurance Fund) in 2011-12, $1.1 million in 2012-13 and $100,000 ongoing, to fund 10.0 positions (8.0 two-year limited-term, 1.0 one-year limited-term, and 1.0 ongoing) to address new workload associated with the review of health insurance rate filings as a result of Chapter 661, Statutes of 2010 (SB 1163).

Background. Chapter 661 amends the law regulating health care service plans and health insurers in order to ensure that both the DMHC and CDI have the authority necessary to review the rate filings for all markets consistent with the requirements of the PPACA. The new workload consists of expanded scope and extent of the actuarial review to be undertaken by CDI, and new actuarial reporting and data trend analysis requirements.

Issue 1.b – Health Care Coverage (AB 2470)

Governor's Budget Request. The Governor requests $642,000 (Insurance Fund) in 2011-12, and $602,000 in 2012-13, to fund 6.0 Staff Counsel positions on a two-year limited-term basis to support the additional rate filings and new cancellation and non-renewal appeal process as a result of Chapter 658, Statutes of 2010 (AB 2470).

Background. Chapter 658: (1) imposes new requirements on an insurers' ability to cancel, rescind, and non-renew health insurance policies; (2) creates a system whereby the Commissioner will review the propriety of cancellations, rescissions, and non-renewals where the insured has complained with the insurer being entitled to a hearing; and (3) provides a mechanism for a policyholder, certificate holder, or other insured who alleges that a policy or coverage has been or will be cancelled, rescinded, or not renewed in violation of law to require a review by the Commissioner. This request will provide the resources to implement new workload required by Chapter 658 regarding industry cancellation, rescission, and non-renewal practices and to provide policyholders with the required review mechanisms.

Issue 1.c – Health Benefit Exchange (SB 900 and AB 1602)

Governor's Budget Request. The Governor requests $107,000 (Insurance Fund) in 2011-12, and $100,000 in 2012-13, to fund one staff counsel position on a two-year limited-term basis to support the additional policy form review activities required as a result of the implementation of the California Health Benefits Exchange established by Chapters 659 and 655, Statutes of 2010 (SB 900 and AB 1602, respectively).

Background. Chapter 659: (1) creates the California Health Benefits Exchange (Exchange), an independent public entity, and delineates its composition and the operation of the executive board of the Exchange, and (2) requires a review of the federal Health and Human Service internet portal prior to January 1, 2015, to determine whether it provides sufficient information to facilitate fair and affirmative marketing of all individual and small employer health insurance. If the review determines the federal portal to be inadequate, Chapter 659 requires the establishment and maintenance of an electronic clearinghouse.

Chapter 655 enacts the California Patient Protection and Affordable Care Act, and provides the Exchange with operational authority, as well as authority to implement the Exchange and navigator provisions of the PPACA by 2014.

Staff Comment. With the exception of one the ongoing position included in request Health Insurance Premium Rate (SB 1163), these three budget requests represent limited-term resources. This is appropriate, as the full extent of the workload related to PPACA and changes in state law is not fully known. By approving these requests as limited-term, the Legislature can review the workload and ensure the appropriate budget resources are provided in future budget cycles. Additionally, staff notes that approving the resources as limited-term will also allow time for study and analysis of whether or not California wants to continue to have two departments, DMHC and CDI, regulating the insurance market.

Staff Recommendation: Approve the budget requests; with regard to request Health Insurance Benefit Premium (SB 1163), staff recommends that the position proposed as ongoing instead be approved as two-year limited-term.

Vote: Staff recommendation approved 2-1; Senator La Malfa voting no.

Issue 2 – Department of Insurance Workload Resource Augmentation

Governor's Budget Request. The Governor requests an increase of $7.9 million (Insurance Fund) in 2011-12, and $7.0 million ongoing, to fund 54.0 positions to address increased workload while continuing to meet statutory mandates.

Background. The CDI reports that its workload has increased in recent years without a commensurate increase in staffing resources. Further, in 2009-10 the CDI budget was permanently reduced by $17.4 million through a line-item veto action. As a result of this reduction, CDI reports that backlogs are increasing throughout the department, including in the Rate Regulation Branch, which has a backlog of 1,080 files; the Field Examination Division, which has examined only two title companies compared to 19 in 2008; and, the Consumer Services Division, where complaints have increased 11 percent and complex health insurance complaints have increased 118 percent. CDI indicates that the resources in this request will not eliminate the backlog throughout the department. Rather, the resources will allow the Department to address the backlog and then remain even with workload going forward. CDI proposes to apportion the resources in this request as follows:

Division	2010-11 Positions	2011-12 New Positions	2011-12 Add'l Funding
Rate Regulation	88.0	2.0	268,000
Financial Surveillance	161.0	5.0	774,000
Executive	26.0	2.0	156,000
Consumer Services & Market Conduct	151.0	10.0	1,175,000
Investigation	92.0	6.0	1,019,000
Fraud	289.0	14.0	2,931,000
Legal	125.0	14.0	1,492,000
Administration & Licensing	280.0	1.0	121,000
		54.0	**$7,936,000**

Staff Comment. Staff notes that the LAO is currently undertaking a workload analysis of this request and is therefore withholding any recommendation to the Legislature until that analysis is complete. The Subcommittee may wish to wait to consider this request until after the LAO analysis is complete.

Staff Recommendation: Hold open pending receipt of the LAO's workload analysis.

Vote: Budget request approved 2-0; Senator La Malfa abstaining.

0890 SECRETARY OF STATE

Department Overview. The Secretary of State (SOS), a constitutionally established office, is the chief election officer of the state and is responsible for the administration and enforcement of election laws. The SOS is also responsible for the administration and enforcement of laws pertaining to filing documents associated with corporations, limited partnerships, and perfecting security agreements. In addition, the SOS is responsible for the appointment of notaries public, enforcement of notary laws, and preservation of documents and records having historical significance. All documents filed are a matter of public record and of historical importance. They are available through prescribed procedures for public review and to certify authenticity.

Budget Overview. The January Governor's Budget provides the SOS with 505 authorized positions and $161.5 million ($31.1 million GF). This is a decrease of no positions and $10.9 million.

Issues Proposed for Discussion / Vote:

Issue 1 – Help America Vote Act Amended Spending Plan

Governor's Budget Request. The Governor requests expenditure authority of $70 million (federal funds) in 2011-12 to continue implementation of the statewide mandates of the federal Help America Vote Act of 2002 (HAVA).

2010-11 Budget. The 2010-11 budget provided $4.2 million (federal funds) to continue implementation of HAVA-related state mandates, including assistance for individuals with disabilities, voting systems testing/certification, voter education, performance measures, and administration.

Background. Generally speaking, the federal HAVA requires state and localities to meet uniform and nondiscriminatory election technology and administration requirements applicable to federal elections. Federal HAVA funding was originally received by the state in 2003, and a spending plan was required by the Legislature in 2004 and approved in April 2005. The SOS revises the HAVA spending plan annually to accurately reflect actual spending, and propose changes for future spending based on new funding and changes in expenditures.

Of the $70 million (federal funds) included in this request, $66.9 million is proposed as local assistance to counties and $3.2 million is for state operations. Of the $66.9 million in local assistance, $65.9 million is for voting system upgrades and $1.0 million is for elections assistance for individuals with disabilities. The voting system upgrades are required under HAVA to ensure an accessible, voter-verifiable paper audit trail. The state operations funding will be utilized for the continued administration of statewide modernization and replacement of voting equipment; education and training programs for elections officials and poll workers; and, development and dissemination of voting information to increase voter participation and confidence.

Staff Comment. This request does not include funding for the VoteCal project, which is the HAVA-required uniform, centralized, interactive computerized voter registration database that is defined, maintained, and administered at the state level. That request is discussed as Issue 2 below.

Staff Recommendation: Approve the budget request.

Vote: Budget request approved 3-0.

Issue 2 – Help America Vote Act, VoteCal

Governor's Budget Request. The Governor requests expenditure authority of $11.6 million (federal funds) in 2011-12 to continue implementation of VoteCal, the federal Help America Vote Act (HAVA)-required and funded uniform, centralized, interactive computerized voter registration database that is defined, maintained, and administered at the state level.

2010-11 Budget. The 2010-11 budget included $23 million (federal funds) to continue implementation of VoteCal.

Background. Under federal HAVA requirements, VoteCal must coordinate electronically with systems similar to the one used by the Department of Motor Vehicles, the Department of Health Care Services, and the Department of Corrections and Rehabilitation for identification and list maintenance purposes. VoteCal must also provide a functional interface for counties. California reached an interim solution to satisfy the requirements of HAVA, but must achieve a long-term solution per an agreement with the U.S. Department of Justice. VoteCal is that solution.

Staff Comment. The 2011-12 request is consistent with previous updates and continues to appropriately administer the HAVA-required VoteCal system. Staff notes, however, that due to the fact that the initial system integration (SI) vendor failed to provide the contractually required performance bond, which required the SOS to terminate the contract in May 2010, the SOS now estimates that the VoteCal project will be extended until June 2014. This is 1.25 years beyond the previously projected and approved February 2012 completion date. The greatest impact on the schedule is the 16 months it will take to sign a contract with a new SI vendor. Approximately $6.6 million of the resources included in this request are for payment to the SI vendor in 2011-12. Due to the re-procurement delay, it is highly unlikely that these funds will be fully expended in 2011-12, but staff notes that the allocation level is within the parameters of the approved project documents. Further, it would be difficult at best to estimate the 2011-12 SI vendor costs and, in any case, the unused federal funds will roll forward to 2012-13 and be reflected in a budget request for that fiscal year.

Staff Recommendation: Approve the budget request.

Vote: Budget request approved 2-0; Senator La Malfa abstaining.

2320 DEPARTMENT OF REAL ESTATE

Department Overview. A primary objective of the Department of Real Estate (DRE) is to protect the public in real estate transactions and provide licensing, regulatory, and subdivision services to the real estate industries. The DRE is entirely special funded (Real Estate Fund) and derives its revenues from examination, license, and subdivision fees. The core functions of the DRE are to administer license examinations, issue real estate licenses, regulate real estate licensees, and qualify subdivision offerings.

Budget Overview. The January Governor's Budget provides DRE with 381 authorized positions and $46.0 million (RE Fund and reimbursements). This is an increase of two positions and $1.5 million.

Issue Proposed for Discussion / Vote:

Issue 1 – SB 36 Mortgage Loan Originator Licensure (SAFE Act)

Governor's Budget Request. The Governor requests $216,000 (Real Estate Fund) and two positions for continued implementation of the federally mandated Secure and Fair Enforcement Licensing Act of 2008 (SAFE Act) which requires states to implement a new licensing program for mortgage loan originators (MLOs).

2010-11 Budget. The 2010-11 budget included $2.8 million (Real Estate Fund) and 27 positions to begin implementation of the SAFE Act.

Background. The federally mandated SAFE Act requires all states to license and register their MLOs through a nationwide registry called the National Mortgage Licensing System (NMLS). Chapter 160, Statutes of 2009 (SB 36), brought California into compliance with the SAFE Act by requiring those engaging in MLO activities to obtain a license from the Department of Corporations or, if a real estate licensee, obtain a license endorsement from the DRE.

The SAFE Act requirements are similar to, but somewhat different from, the requirements for licensure under California's Real Estate Law. At this point in the SAFE Act implementation process, the main drivers of new licensing and enforcement workload for the DRE will be the MLO notification process and the annual Business Activities Report requirement for all MLO brokers. The amount of new workload will be driven by the number of NMLS registrants; as of December 31, 2010, an estimated 37,373 individuals and over 6,133 real estate companies who perform MLO activities registered on NMLS. The DRE expects additional late registration activity, as licensees become aware of the NMLS registration requirement.

DRE reports that it will be able to comply with existing SB 36 requirements with the resources in this request. However, because DRE is only now compiling final workload data based on the total number of licensees who registered on the NMLS, and the complexity of licensing and enforcement is better known, DRE indicates that this request is a precursor to an additional request for positions, technology enhancements, and budget authority in a Spring 2011 Budget Letter.

Staff Comment. In approving SB 36, the Legislature approached SAFE Act compliance in a narrow sense by requiring a new endorsement on existing real estate licenses. Licensees pay a $300 fee for that endorsement. Staff notes that while this approach has resulted in the least disruption to existing systems and minimized compliance costs to both the state and licensees, the SAFE Act has represented, and will continue to represent, new workload for DRE.

However, as noted above, DRE indicates that a Spring 2011 Budget Letter is planned to request budget authority and positions beyond that contained in this request. Additionally, DRE faces a facility issue which remains unresolved from 2009-10. Last year, this Subcommittee specifically requested that DRE present a formal request during the 2011-12 budget process to ensure that DRE did not absorb the costs of relocating and consolidating its Sacramento facilities within its existing budget, an action that could result in decreased enforcement and consumer protection activities. DRE indicates that it plans to present a separate Spring 2011 Budget Letter for the Sacramento headquarters move costs. Finally, staff notes that the Senate Business and Professions Committee is holding an oversight hearing on February 28, 2011, focused on DRE enforcement and consumer protection issues. Given these factors, staff recommends that this request be denied without prejudice and instead wait to consider this request in the context of the Spring 2011 requests from DRE, as well as the findings from the Senate Business and Professions Committee oversight hearing.

Staff Recommendation: Deny the budget request without prejudice; consider during the Spring 2011 budget process.

Vote: Budget request denied without prejudice 3-0; Subcommittee will consider during the 2011 budget process.

STATE OPERATIONS EFFICIENCIES

Issue Proposed for Discussion Only

Issue 1 – State Operations Efficiencies

Governor's Budget Request. The January Governor's Budget includes $363 million ($200 million GF) in savings associated with identification of efficiencies in state operations, including identification of agencies, departments, and programs that can be reorganized to eliminate duplication and unnecessary functions; review of state peace officer and safety classifications; and reductions in other areas like contracting, fleet operations, and cell phone use.

Background. The Governor's January budget begins what is described as an ongoing effort to make state government more effective and efficient by reducing costs, improving timelines, and reducing overlapping responsibilities. In 2010-11, the Governor has taken steps to accomplish these goals by taking the following actions: (1) eliminating the Office of the Secretary of Education; (2) eliminating the American Recovery and Reinvestment Act Inspector General and transferring ongoing work to other established oversight entities, including the Bureau of State Audits and State Controller's Office; and (3) reducing the Governor's Office budget by 25 percent. Additional 2010-11 savings were achieved by spending only $120,000 of the $770,000 budgeted for transition costs.

Separately, the Governor has directed agency secretaries and department directors to immediately review their operational costs and identify options to generate savings. Two immediate areas of focus are use of cell phones by state employees and the number of state vehicles:

1. With regard to cell phones, the state currently pays for approximately 96,000 cell phones, one for over 40 percent of all state employees. Via an Executive Order issued on January 11, 2011, the Governor ordered all agency secretaries and department directors to: (1) document and review all authorized cell phone and smart phone procurement and related phone, data, internet and other usage plans for and by their employees and (2) identify and implement by June 1, 2011, cuts sufficient to meet or exceed a 50 percent decrease in the number of cell phones and smart phones for which the state is currently responsible and achieve at least $20 million (all funds) in savings.

2. With regard to the state fleet, which totals 13,600 vehicles (not including some 12,000 vehicles that are used for public safety), the Administration indicates it will reduce the number of vehicles the state maintains by requiring each vehicle's purpose and necessity to be rejustified. Only vehicles necessary for critical state functions will be retained, and only when retaining such vehicles is cost effective.

The mechanism to achieve these savings is Control Section 3.91, which requires that the Director of Finance allocate the reductions necessary to each item of appropriation in the budget to accomplish the required savings.

Staff Comment. The overarching goal of seeking greater efficiency and effectiveness in state operations is worthwhile. By beginning with cell/smart phones and fleet management, the Administration has identified two areas which will likely bear some fruit. Staff understands that the Administration has a “living list” of additional areas of exploration, including micro items such as toll-free telephone lines and macro items such as executive branch reorganization plans. At some point, this list will have to be narrowed, or triaged, to permit the focused work to occur to build to the point where real savings are achieved in 2011-12.

Committee Questions. Based on the above comments, the Committee may wish the Administration to provide responses to the following questions:

1. What other specific areas is the Administration currently considering for increased efficiency and effectiveness?
2. What is the timeframe for this process?
3. How can the Legislature be of assistance to the Administration in this process?

Staff Recommendation: No action; information item only.

ATTACHMENT 1

Differences Between the Federal Affordable Care Act and 2010 California Health Reform Legislation That Have a Workload Impact on the Department of Insurance

	Federal	State
SB 1163: Rate Review		
Individual/Small Group rate filings	Only rate increases in excess of 10% must be filed. (45 CFR 154.200), does not apply to grandfathered plans. (45 CFR 154.103(b))	**All** individual and small group rates must be filed. (IC 10181.3(a))
Data required in filing	18 elements (45 CFR 154.210(e),(g))	25 elements (e.g., IC 10181.3(b))
Examples of differences in data requirements:		
Trend projections	Utilization, service/unit co st (45 CFR 154.215(e)(2))	Utilization, price inflation, fees and risk, broken down into 7 aggregate benefit categories (e.g., IC 10181.3(b)(19))
Cost containment/quality improvement data	Not required	Required (e.g.: IC 10181.2(b))
Actuarial certification by outside actuary	Not required	Required (IC 10181.6)
Criteria re: independence of outside actuary	Not required	Required. CDI will have to evaluate.
Filing must be actuarially sound	Not required	Required (IC 10181.6). CDI will have to evaluate.
Aggregate Reporting Requirements	Medical loss ratio data (45 CFR 158.110-170)	9 data elements, not including medical loss ratio (IC 10181.3(c), 10181.4(c))
Carrier-provider contract rates	Not discussed	Received by CDI, must be segregated, kept confidential. (IC 10181.7(b))
Actions Required of CDI	Receive filings (PPACA 2794), provide information to HHS, including premium trends (PPACA 2794(b),(c))	CDI must review filings to detect violations (IC 10181.11), CDI must make findings regarding rate justifications and post on website (IC 10181.11(f)),CDI must make all submitted information public (IC 10181.7(a)), CDI must make quarterly reports to Legislature (IC 10181.11(d)).

AB 2470: Cancellation/Nonrenewal/ Rescission		
Applicable to non-renewal?	No. Applies only to rescission. (PPACA 2712)	Applies to rescission, cancellation, non-renewal (IC 10273.4(b)). Expanded scope means expanded CDI policy form review beyond federal requirements.
CDI review and hearing process for cancellations, rescission, non-renewal	Not required in federal law.	Requires CDI to establish a process to review complaints to determine adequacy, reinstate coverage, and a hearing process for carrier appeals.
SB 900/AB 1602: Exchange		
Review of Exchange policy forms by CDI	Required if federal government operates exchange	Required if state operates exchange
Include California health mandates	California mandates not required.	State has option to include California mandates in Exchange policies, which increases complexity of policy review.
Plans offered	Policies offered in exchange need not all be offered outside exchange.	All policies offered inside exchange must also be offered outside exchange (IC 10112.3 (c)). Increases CDI review load.
Federal Internet Portal	Maintained by HHS	CDI & DMHC must review HHS site to determine if meets requirement for affirmative marketing, especially outside exchange. If inadequate, CDI & DMHC must establish clearinghouse.
Catastrophic coverage	Carriers that do not participate in Exchange may sell catastrophic coverage	Carriers that do not participate in exchange cannot sell catastrophic coverage (IC 10112.3(d)). Adds additional element to CDI market conduct examinations.

Bruce Hinze, January 22, 2011

Senate Budget and Fiscal Review—Mark Leno, Chair

SUBCOMMITTEE NO. 4 Agenda

Senator Michael J. Rubio, Chair
Senator Noreen Evans
Senator Doug LaMalfa

Thursday, January 27, 2011
9:30 a.m. or Upon Adjournment of Session
Room 112

Consultant: Kris Kuzmich

Item Number and Title

1700	Department of Fair Employment and Housing
1760	Department of General Services
2240	Department of Housing and Community Development
8860	Department of Finance, California Recovery Task Force
8940	Military Department

(See Table of Contents on page 2 for a More Specific Listing of Issues)

Pursuant to the Americans with Disabilities Act, individuals who, because of a disability, need special assistance to attend or participate in a Senate Committee hearing, or in connection with other Senate services, may request assistance at the Senate Rules Committee, 1020 N Street, Suite 255 or by calling 916-324-9335. Requests should be made one week in advance whenever possible.

AGENDA – VOTE ONLY ITEMS

(Please see summary chart on Page 3)

AGENDA – DISCUSSION / VOTE ITEMS

Issues Proposed for Vote Only:

	Issue	2011-12 Amount	Fund Source	Staff Recommendation
	8940 Military Department			
1	Custodian for Dublin Readiness Center and Field Maintenance Shop	$67,000 total and one position*	$17,000 GF $50,000 Federal Funds	APPROVE
2	State Active Duty Employee Compensation Increase	$1.363 million	$705,000 GF $658,000 Federal Funds	APPROVE
3	Military Department Environmental Programs Increase to Meet Federal Requirements	$413,000 and four positions*	Federal Funds	APPROVE
4	Military Department Civil Support Planning Positions and Interoperable Communications Equipment	$1.0 million and four positions*	Reimbursements	APPROVE
5	CalEMA Homeland Security Training and Exercise Program	$5.1 million and 33 three-year limited-term positions	Reimbursements	APPROVE
6	Quality Assurance Representatives	$393,000 and four positions*	Federal Funds	APPROVE

**All positions are absorbed from within the Military Department's existing budget; therefore, no net increase in positions will result from these requests.*

Vote:

Issues Proposed for Vote Only – Issue Descriptions

8940 MILITARY DEPARTMENT

For overview and budget information regarding this department, please see page 15 of this agenda.

Issue 1 – Custodian for Dublin Readiness Center and Field Maintenance Shop

Governor's Budget Request. The Governor requests increased expenditure authority of $67,000 ($17,000 GF and $50,000 federal funds) for a custodian to support the new Dublin Readiness Center and Field Maintenance Shop located at Parks Reserve Forces Training Area.

Background. The Military Department's state and federal mission require fully functional armories and maintenance facilities to meet readiness, support its full-time workforce, and provide emergency community support. The Dublin Readiness Center is scheduled for completion by May 2011; the Field Maintenance Shop was completed in December 2008. The federal government provided 100 percent of the construction funds for the Dublin facilities. The state's responsibility is to ensure the facilities are operational and maintained to meet mission requirements. The one custodian position required for this request will be absorbed from within the Military Department. The $17,000 GF used for this position will come from the armory maintenance program, which currently funds a combination of maintenance personnel and maintenance work.

Issue 2 – State Active Duty Employee Compensation Increase

Governor's Budget Request. The Governor requests a baseline augmentation of $1.363 million ($705,000 GF and $658,000 Federal Trust Fund) to cover the State Active Duty (SAD) compensation increases to be granted effective January 1, 2011, and estimated to be granted January 2, 2012.

Staff Comment. Per state statute, pay for SAD employees must be based upon military pay increases granted by Congress; additional compensation adjustments are also mandated due to a congressionally-approved increase in the military allowance for housing and subsistence. The 2011-12 estimates are 1.9 percent for salary and 1.5 percent basic allocation for housing.

Issue 3 – Military Department Environmental Programs Increase to Meet Federal Requirements

Governor's Budget Request. The Governor requests increased expenditure authority of $413,000 (federal funds) and four positions to support increasing environmental requirements within the Environmental Program Directorate.

Background. The California Army National Guard has numerous facilities throughout the state, including three major training bases covering over 50,000 acres; an aviation repair depot servicing military helicopters from 13 western states; three aviation support facilities; two equipment storage sites for armored combat vehicles; two major vehicle and weapons maintenance centers; 34 smaller vehicle maintenance shops; supply depots; and forward operating bases. For these units to be effective, they must be in compliance with all federal, state, and local environmental laws, as well as Department of Defense Instructions and Army regulations. The four positions would come at no cost to the state as they are 100 percent federally funded by the National Guard Bureau through a Master Cooperative Agreement with the state. The four positions required for this augmentation will be absorbed from within the Department and will be responsible for making sure federal construction projects can be executed in California.

Issue 4 – Military Department Civil Support Planning Positions and Interoperable Communications Equipment

Governor's Budget Request. The Governor requests increased expenditure authority of $1.0 million (reimbursements) in support of State Homeland Security Grant Program funds for emergency planning, immediate emergency response and exercise Homeland Security planning, and procurement of emergency equipment to support the Governor's Office and the California Emergency Management Agency.

Background. This request provides the Military Department with functional staff to cover the full spectrum of Homeland Security emergency planning, exercises, and operations and is critical to executing a coordinated and rapid emergency response while maintaining Continuity of Operations and Continuity of Government plans. Of the expenditure authority requested, $635,000 will enable the Department to hire four personnel to fill required assignments in operations and plans, training and exercises, operational law, and operational logistics. These positions will be absorbed from within the Department. The remaining $383,000 will be used to purchase communications equipment to allow California National Guard forces/assets a greatly increased capability to conduct interoperable communications with civilian emergency responders.

Issue 5 – CalEMA Homeland Security Training and Exercise Program

Governor's Budget Request. The Governor requests continuation of reimbursement authority in 2011-12 of $5.1 million (reimbursements) and the re-establishment of 33 three-year limited-term positions to execute an interagency agreement between the Military Department and the California Emergency Management Agency (CalEMA) for staffing support and operating expenses. The source of funds is the federally-funded Homeland Security Grant Program (HSGP).

Background. In 2003, the Military Department was assigned the responsibility of "Executive Agent" by CalEMA for all homeland security terrorism training and exercise activities funded from the various initiatives that constitute the federal HSGP. In this capacity, the CalEMA Homeland Security Training and Exercise Program (HSTEP), consisting of the Military Department and various federal, state, and local agency staff, was charged with providing statewide oversight for the training and exercise needs of California's first responder community to respond to terrorist attacks involving weapons of mass destruction. The 33 positions were originally established on a limited-term basis for purposes of the interagency agreement between the Military Department and CalEMA and all expire on June 30, 2011. These positions provide the necessary Military Department personnel to CalEMA to manage its statewide terrorism training and exercise programs for Weapons of Mass Destruction. These funds also allow for operating expenses related to the HSTEP. The proposed funding level in 2011-12 represents a reduced reimbursement level from the previous five years (from $7.5 million to $5.1 million); this is a result of a reduction in contracts for loaned executives from other governmental agencies that have been assigned to the HSTEP.

Issue 6 – Quality Assurance Representatives

Governor's Budget Request. The Governor requests increased expenditure authority of $393,000 (federal funds) for four Quality Assurance Representatives to provide on-site quality assurance and observation support to the Facilities Directorate project managers on renovation and construction projects statewide, and to help ensure that construction projects at Military Department facilities are executed in compliance with relevant building codes, specifications, and plans.

Background. The Military Department's Directorate of Facilities currently employs 14 Quality Assurance Representatives (e.g., inspectors) who provide on-site construction observation support to new construction and renovation projects at departmental readiness centers, maintenance shops, and training bases statewide. At present, a Quality Assurance Representative is typically responsible for between two and four concurrent projects, requiring each Representative to split his time between work sites. As a result, at least some work at each project site is completed un-observed by a Representative. Federal Corps of Engineers standards require that a Quality Assurance Representative be on site whenever work is being performed. The resources in this request, which are 100 percent federally-funded, will ensure federal inspection standards are met. These four positions will be absorbed from within the Department.

8860 DEPARTMENT OF FINANCE, CALIFORNIA RECOVERY TASK FORCE

Overview. On February 17, 2009, President Obama signed the American Recovery and Reinvestment Act (ARRA), a $787 billion federally-funded economic stimulus plan for a wide range of federal, state, and local programs as well as tax relief for qualified businesses and individuals. ARRA also created new requirements for state-level oversight and reporting of stimulus dollars provided to state entities.

Both the 2009-10 and 2010-11 budgets provided funding for California's ARRA accountability framework, comprised of four organizational components: the California Recovery Task Force (CRTF); the ARRA Inspector General (ARRA IG); the Bureau of State Audits (BSA); and, the State Controller's Office (SCO). Both the BSA and SCO were pre-existing entities, while the CRTF and ARRA IG were established via Executive Order by the Governor in Spring 2009.

In January 2011, Governor Brown announced he was eliminating the ARRA IG's Office six months early (funding for that office in the 2010-11 budget was provided on a one-year limited-term basis). Any outstanding audit activities of that office were transferred to the SCO or BSA.

Issue Proposed for Discussion / Vote:

Issue 1 – California Recovery Task Force – ARRA Funds Oversight

Governor's Budget Request. The Governor requests one-time funds totaling $1.6 million ($928,000 GF and $700,000 Central Service Cost Recovery Fund) to support oversight and reporting for remaining ARRA funds in 2011-12. In addition to supporting the California Recovery Task Force (CRTF), the resources in this request will also provide funding for the California Technology Agency (CaTA) and support staff at Department of Finance [Office of State Audits and Evaluations (OSAE) and Fiscal Systems Consulting Unit (FSCU)], providing information technology activities related to federally-required quarterly reports and continued audit support, respectively. Figure 1 below illustrates funding levels for the three entities comprising the CRTF generally:

Figure 1

	2010-11	**2011-12 Funding**
California Recovery Task Force	$1,700,000	$578,000
California Technology Agency	$1,400,000	$600,000
Department of Finance: (1) Office of State Audits and Evaluations; and, (2) Fiscal Systems Consulting Unit	$905,000	$450,000
TOTAL	**$4,005,000**	**$1,628,000**

**Note, the fund split is 57 percent GF and 43 percent Central Service Cost Recovery Fund.*

Background. The primary functions that remain in 2011-12 will be quarterly reporting, compliance monitoring, and ensuring that all deadlines related to retaining ARRA funds are met to avoid losing any money awarded due to failure to spend funds within the required timeframes or for other non-compliance issues. CRTF responsibilities diminish as funds are expended; therefore, this proposal significantly reduces the staffing of the CRTF to oversee the remaining ARRA funds and to provide continued quarterly reports. In September 2010, 1,121 ARRA grants remained; in 2011-12, that number will drop to 568 grants.

The CaTA is responsible for ongoing maintenance of the California ARRA and Accountability Tool (CAAT), the state's centralized reporting database. The CAAT tool provides a vehicle for departments to submit and report the data, but is only one component of the information technology (IT) required to report the information to the federal government and citizens of the state. In 2011-12, the CaTA will transition from contract/consultant staff on the CAAT system to utilization of state staff. The State IT staff will fully support and maintain the IT infrastructure (hardware, software, and connectivity), the multitude of user accounts, and provide end-user support for the ongoing reporting. Currently, there are over 300 registered users uploading over 1,100 reports consisting of thousands of records to the system in multiple formats. There will be savings realized in 2011-12 as the maintenance and support is transitioned from contractor resources to state staff, however CAAT requires continuous support and maintenance due to the complexity of the system and the continued reporting to the federal government. The funding for position support will be absorbed within the CaTA.

Staff Comment. The proposed resources for the CRTF in 2011-12 have been reduced from the level provided in 2010-11 reflective of the declining workload. However, staff notes that this request includes 5.1 positions for the CRTF itself and 4.9 borrowed staff from the Department of Finance. This level of staffing is still potentially excessive given that the workload now consists primarily of recipient reporting to the CAAT which is administered by the CaTA. Additionally, given that 57 percent of this request is funded by the GF, close scrutiny is warranted to ensure that the staffing resources provided match the workload.

Staff Recommendation: Hold open pending receipt of additional workload information.

Vote:

1700 DEPARTMENT OF FAIR EMPLOYMENT AND HOUSING
1760 DEPARTMENT OF GENERAL SERVICES

Department Overview. The Department of Fair Employment and Housing (DFEH) is responsible for protecting the people of California from unlawful discrimination in employment, housing, and public accommodations, and from the perpetration of acts of hate violence. The Department's jurisdiction extends to individuals, private or public entities, housing providers, and business establishments within the State of California.

Budget Overview. The January Governor's Budget provides the DFEH with 197 authorized positions and $21.7 million ($16.2 million GF).

In 2010-11, the DFEH consisted of 207 authorized positions, including ten positions (eight positions in headquarters including the Chief Information Officer, one position in southern California, and one position in the Bay Area) which were used to provide information technology (IT) services for the department and 150 positions in the department's enforcement division. Three of the IT positions were eliminated as part of the DFEH's workforce cap reduction, leaving seven remaining authorized positions to support IT workload.

Issue Proposed for Discussion / Vote:

Issue 1 – Information Technology Transfer to Department of General Services; Retain Two Positions for Enforcement

Governor's Budget Request. The Governor requests to permanently transfer DFEH's Information Technology (IT) function and five positions to the Department of General Services (DGS) and proposes budget provisional language that sets aside $507,000 GF from DFEH to pay for the transferred functions. In addition, the Governor proposes to redirect the two remaining IT positions to DFEH's enforcement division on a two-year limited-term basis to process claims resulting from the settlement of a class-action lawsuit.

Background. The DFEH entered into an agreement with the DGS effective July 2010 which transferred DFEH's entire IT function and five positions to DGS's IT unit and provided $465,000 to DGS for the cost of providing these services in 2010-11. One objective of this agreement was to achieve efficiency and cost savings.

In September 2010, DFEH reached its first multi-million dollar discrimination settlement, totaling more than $6.9 million. According to the DFEH, the settlement will result in a significant increase in workload. The DFEH, therefore, is proposing to retain the two remaining IT positions and convert them into two-year limited-term positions in its Special Investigations Unit to address expected new workload stemming from the settlement of 1,500 family leave claims. All claims are required to be submitted by February 15, 2011. Shortly thereafter, the designated third-party administrator will submit all timely and valid claim forms to DFEH and DFEH staff will then conduct an independent evaluation of each claim to determine whether, on a case-by-case basis, the claimant experienced a California Family Rights Act violation and, if so the type of violation and the appropriate level of damages.

LAO Comment. Centralizing the DFEH's IT function within DGS is reasonable. However, transferring the five positions from DFEH to DGS without having DGS justify the need for these additional staff reduces transparency may not accurately reflect the new workload. If DGS is unable to absorb the increased workload, then it can request the appropriate level of additional staff and provide workload justification.

The DFEH is also requesting to redirect two positions from its former IT unit to its enforcement division to handle the workload related to the settlement of the class-action lawsuit. At the time this request was prepared, the volume of claims that would need to be processed was unknown. The DFEH indicates that it will know the total number of settlement claims filed by mid-February and be able to better describe its workload needs then. In addition, given that pursuing large class action settlements, rather than individual claims, is a relatively new effort for the DFEH, the LAO continues to examine this request. The LAO has also raised questions to DFEH about which party should be responsible for paying the related administrative costs when administering a large settlement.

LAO Recommendation. We recommend the Legislature adopt the Governor's 2011-12 January budget proposal to transfer the DFEH's IT workload to the DGS. However, the Legislature should reject the transfer of five positions to DGS and $507,000 GF to pay for these staff. Instead, the LAO recommends elimination of the five positions at DFEH and that the Legislature require DGS to justify the need for additional staff on a workload basis. Should DGS incur additional costs, DFEH should provide the appropriate level of reimbursements to fund this workload. In addition, the LAO recommends the Legislature withhold approval of redirecting two positions from DFEH's IT unit to its enforcement division until the volume of the new workload is better known. The LAO continues to examine what would be the most appropriate source of funding for this workload.

Staff Comment. Staff concurs with the LAO assessment that workload justifications are necessary before the Legislature can approve the request for: (1) DFEH to retain two positions for enforcement; and (2) DFEH to provide reimbursement to DGS for the cost of DGS providing IT functions to DFEH. Otherwise, the resources provided, particularly with regard to the reimbursement between DFEH and DGS, could be greater than is warranted. This is particularly important if the Administration is considering transferring IT workload from other small departments to DGS. Establishing a precedent here where inefficiencies are imbedded in the reimbursement level should be avoided. Additionally, it is worth noting that DFEH is 75 percent funded by the GF.

Staff Recommendation. Staff recommends the following:

1. Approve the transfer of the DFEH IT function and workload to DGS;
2. Sweep the excess five positions at DGS that could be redirected to the transferred DFEH function as well as the $300,000 Service Revolving Fund; and,
3. Hold open the: (a) DFEH request to retain the two positions, and (b) DFEH providing reimbursement to DGS for the transferred IT function; consider both of these aspects of the request at the Subcommittee's February 10, 2011, "open issues" hearing, after both DGS and DFEH submit workload justifications supporting the transferred IT function and additional enforcement activities, respectively.

Vote:

1760 DEPARTMENT OF GENERAL SERVICES

Department Overview. The Department of General Services (DGS) provides management review and support services to state departments. The DGS is responsible for the planning, acquisition, design, construction, maintenance, and operation of the state's office space and properties. It is also responsible for the procurement of materials, data processing services, communication, transportation, printing, and security.

Budget Overview. The January Governor's Budget provides the DGS with 3,923.8 authorized positions and $1.1 billion ($5.5 million GF). This is a decrease of eight positions and $18.5 million. As a central service agency, the vast majority of DGS' budget is comprised of special fund and reimbursement revenue, received for services performed for other state departments and agencies.

Issue Proposed for Discussion / Vote:

Issue 1 – Office of Public School Construction, Emergency Repair Program

Governor's Budget Request. The Governor proposes a state operations reduction of $247,000 GF and 1.9 positions for the Office of Public School Construction (OPSC) administration of the Emergency Repair Program (ERP) in 2011-12. This request will conform OPSC budget resources to the remaining workload needs of the ERP.

Background. As a part of the *Williams vs. State of California* settlement [Chapter 899, Statutes of 2004 (SB 6)], the ERP was established to provide a total of $800 million for the purpose of addressing emergency facilities needs at school sites in deciles 1 through 3. To date, the OPSC has processed approximately $510 million in applications, of which approximately $338 million Proposition 98 GF has received funding. The OPSC has received applications from eligible school districts at a level that, once processed and funded, will fulfill the State's obligations pursuant to the terms of the *Williams* settlement. More specifically, the OPSC will require 2.9 PYs and $280,000 in 2010-11, and 1.0 PYs and $93,000 in 2011-12, to process the approximately $290 million remaining applications. No workload will remain for the ERP once applications are processed up to the $800 million funding level specified in the *Williams* settlement.

Staff Comment. Staff notes no issue with the content of this request; it is consistent with a recent vote of the State Allocation Board (SAB), which directs the work of the OPSC, to stop accepting ERP applications due to the program reaching its expenditure level. However, staff notes that on process this request fails to meet a clear directive provided by this Subcommittee last year when, considering several OPSC requests, it clearly stated that future OPSC budget requests needed to be reviewed by the SAB per Education Code Section 17070.65 and prior to their being included in the Governor's budget. In approving this state operations reduction, the Subcommittee may wish to again restate its concern that the Administration is not consulting with the SAB regarding the OPSC's budget.

Staff Recommendation: Approve the state operations budget reduction.

Vote:

2240 DEPARTMENT OF HOUSING AND COMMUNITY DEVELOPMENT

Department Overview. A primary objective of the Department of Housing and Community Development (HCD) is to expand housing opportunities for all Californians. The Department administers housing finance, economic development, and rehabilitation programs with emphasis on meeting the shelter needs of low-income persons and families, and other special needs groups. It also administers and implements building codes, manages mobilehome registration and titling, and enforces construction standards for mobilehomes.

Budget Overview. The January Governor's Budget provides the HCD 598.6 authorized positions and $256.0 million ($8.8 million GF). This is a decrease of 6.5 positions and $490.0 million.

The majority of the HCD's expenditures are supported by general obligation bond revenue. The budget includes no bond appropriation authority in 2011-12 (discussed as Issue 2 below). Even without this appropriation, HCD's budget has been steadily decreasing in recent years due to the pending exhaustion of housing bond funds.

Issues Proposed for Discussion / Vote:

Issue 1 – Community Development Block Grant Service Funding Adjustment

Governor's Budget Request. The Governor requests a shift of $1.1 million in federal budget authority from State Operations to Local Assistance and a reduction of ten positions for the Community Development Block Grant (CDBG) program to reflect a correction in federally allowable administrative costs. To accommodate the reduced level of program administration funding, HCD plans to: (1) reduce the number of awards for the Planning and Technical Assistance and Enterprise Fund Categories of the CDBG program; and, (2) decrease the number of awards in the CDBG General portion of the program by increasing the average award.

Background. HCD's CDBG program was created over twenty-eight years ago to address the fact that California's non-entitlement jurisdictions, which are smaller communities (many of which are rural and economically distressed), lack the resources and/or economies of scale to receive, award, and monitor these federal grants in an efficient and effective manner that allocates the funds to the most pressing needs, meets all federal requirements, and protects against fraud. Presently, HCD's CDBG program serves 168 non-entitlement jurisdictions. By consolidating the administration of the CDBG program for these communities into HCD, the state gains substantial economies of scale and program effectiveness, reducing the number of staff that need to be trained, and gaining the ability to target the most pressing needs across all of the eligible communities.

Although HCD has authority for 28 positions, the federal funds available to the department is only sufficient to support 18 of those positions. The source of the current problem is a combination of short- and long-term factors and some recent issues regarding the funding for the HCD administration of the CDBG program, including: (1) the complexity and scope of the Program makes it labor intensive to administer; (2) the federal allowance for State administration costs for the Program is minimal; and, (3) the $1.1 million increase in the Program budget in 2007-08, which included a shift of $697,000 CDBG program administration funding from GF to federal funds, cannot be sustained due to federal restrictions.

In order to absorb the 30 percent decrease in support dollars, HCD developed the following solution to maintain a viable program at the new program administration funding level:

Workload Driver	Historical Program Level	Proposed Program Level 2011-12	% Change in Activity
Notices of Funding Ability (NOFAs) Offered	6	1	(-) 83.3%
Eligible Activities Offered	81	1	0%
Volume of Awards	112	39	(-) 65.2%
Volume of Activities Requiring Field Monitoring	158	59	(-) 62.7%
Actual Monitoring Site Visits to be Completed	44	20	(-) 54.5%
Jurisdictions Served	66	39	(-) 40.9%

Staff Comment. While the amount of dollars represented in this request are insignificant in comparison to the total funding awarded to non-entitlement communities annually ($1.1 million against an average annual award total of $37 million), it could be argued that the program administration changes the HCD proposes are significant. Administering these funds in one NOFA instead of six per year, restricting eligibility to those jurisdictions that do not have an open grant or have an open grant and have met a 50 percent expenditure requirement, and increasing the award size (which will reduce the overall number of awards) will impact the rural communities that rely on HCD for their CDBG funds. As such, the Subcommittee may wish to defer action on this request to allow time for the impacts of these proposed changes to be fully analyzed and determine if there are other approaches that could be developed that would have less programmatic impact on recipient communities.

Staff Recommendation: Deny the budget request without prejudice; consider during the Spring 2011 budget process.

Vote:

Issue 2 – 2011-12 Housing Bond Appropriation Authority

Governor's Budget Request. The Governor proposes a one-time pause in the issuance of state bonds for new loans and grants for general obligation bond funded projects. This proposal would not affect projects that are already underway, but would impact new loans and grants by potentially delaying them for four to five months. The Administration is proposing this pause to allow time for further analysis of bond sales, the state's overall bonding capacity and debt service obligations, as well as to prioritize allocation of bond resources. This pause will also save an estimated $248 million in GF interest costs.

With regard to HCD, the Governor further proposes that $99 million in new loans and grants for housing projects, which would otherwise be administered by HCD in 2011-12, be suspended independent of any bond sale in 2011-12.

2010-11 Budget. The 2010-11 Budget included several appropriations of Proposition 1C Housing and Emergency Shelter Trust Fund Act of 2006 funds, including: (1) $25 million for the Housing Related Parks Program; (2) $5 million for the Building Equity and Growth in Neighborhoods Program; and (3) $9.275 million in remaining Infill Incentive Grant Program funds.

Background. The Department of Finance indicates that the current General Obligation bond cash balance is sufficient to fund: (1) ongoing projects through December 2011; and (2) new allocations through June 2011 and subsequent cash needs through December 2011. This ensures that no existing bond-funded project will be delayed by the proposed pause in the spring bond sale.

For every other department except HCD, new project allocations in the July through September 2011 period may be delayed for four to five months until the fall bond sale is complete. In the case of HCD, the administration has instead proposed to suspend new loans and grants for housing projects in 2011-12. This would affect programs such as Transit Oriented Development and Housing Related Parks, both of which have a remaining fund balance awaiting appropriation.

Staff Comment. While the pause in the spring bond sale could cause a delay in the jobs/economic development benefit of bond-funded projects being green-lighted, most departments have more bond proceeds than they can spend. As of December 2010, the State Treasurer estimated that the state had about $13 billion in bond proceeds that still had not been spent. So the state would still be spending down that balance and contributing to the economy over the next year even without the spring sale.

Staff notes that the Administration's proposal to suspend HCD housing bond grants in 2011-12 presents a policy question for the Legislature. The net effect of the Administration's proposal is to say that, when the bond sales resume in the fall of 2011, housing grants present no priority for new bond proceeds in 2011-12. Given this, the Subcommittee may wish to act to ensure that housing bonds are given an equal ability to be prioritized and allocated in 2011-12.

Staff Recommendation: Remove Item 2240-401 from the budget bill and adopt placeholder replacement language to authorize HCD to award housing bond funds in 2011-12.

Vote:

8940 MILITARY DEPARTMENT

Department Overview. The California Military Department (CMD) is responsible for the command, leadership, and management of the California Army and Air National Guard and five other related programs. The purpose of the California National Guard (CNG) is to provide military service supporting this state and the nation. The three missions of the CNG are to provide: (1) mission ready forces to the federal government as directed by the President; (2) emergency public safety support to civil authorities as directed by the Governor; and (3) support to the community as approved by proper authorities. The CMD is organized in accordance with federal Departments of the Army and Air Force staffing patterns. In addition to the funding that flows through the State Treasury, the CMD also receives Federal Funding directly from the Department of Defense.

Budget Overview. The January Governor's Budget provides the CMD with 854.5 authorized positions and $144.3 million ($46.0 million GF). This is a decrease of 11.0 positions and an increase of $3.8 million ($1.1 million GF).

Issue Proposed for Discussion / Vote:

Issue 1 – California National Guard Behavioral Health Outreach Liaison Program

Governor's Budget Request. The Governor requests continuation of the California National Guard Behavioral Health Outreach Liaison (BHOL) Program and the three existing positions, funded by $451,000 in Proposition 63 funds.

Background. The BHOL program was authorized in 2009-10 as a pilot program. The BHOL program consists of two licensed clinical staff members and one agency coordinator. These personnel ensure that appropriate mental health information is available for all California National Guard members returning from military deployment. Program staff are responsible for providing training for county and other mental health agency entities throughout California. In addition, BHOL teams coordinate directly with county veteran service officers and mental health officers and continue to integrate the behavioral health programs with the state's Operation Welcome Home program.

Staff Comment. Staff concurs that BHOL is a meritorious program, serving a unique population of National Guard members returning from deployment. These citizen-soldiers are immediately reintegrated back into their communities and families after experiencing posttraumatic events that often have affected the servicemembers' mental health needs. The BHOL program has been operating on a pilot basis; approval of this request would make the program and its staffing permanent within existing funding and staffing levels. Should the Subcommittee approve this request, staff recommends that reporting language be added to collect baseline program data, such as specific program offerings and number of servicemembers served.

Staff Recommendation: Approve the budget request, including reporting language.

Vote:

Senate Budget and Fiscal Review—Mark Leno, Chair

SUBCOMMITTEE NO. 4 Agenda

Senator Michael J. Rubio, Chair
Senator Noreen Evans
Senator Doug LaMalfa

Thursday, January 27, 2011
9:30 a.m. or Upon Adjournment of Session
Room 112

Consultant: Kris Kuzmich

OUTCOMES

Item Number and Title

1700	Department of Fair Employment and Housing
1760	Department of General Services
2240	Department of Housing and Community Development
8860	Department of Finance, California Recovery Task Force
8940	Military Department

(See Table of Contents on page 2 for a More Specific Listing of Issues)

Pursuant to the Americans with Disabilities Act, individuals who, because of a disability, need special assistance to attend or participate in a Senate Committee hearing, or in connection with other Senate services, may request assistance at the Senate Rules Committee, 1020 N Street, Suite 255 or by calling 916-324-9335. Requests should be made one week in advance whenever possible.

AGENDA – VOTE ONLY ITEMS

(Please see summary chart on Page 3)

AGENDA – DISCUSSION / VOTE ITEMS

Issues Proposed for Vote Only:

	Issue	2011-12 Amount	Fund Source	Staff Recommendation
	8940 Military Department			
1	Custodian for Dublin Readiness Center and Field Maintenance Shop	$67,000 total and one position*	$17,000 GF $50,000 Federal Funds	APPROVE
2	State Active Duty Employee Compensation Increase	$1.363 million	$705,000 GF $658,000 Federal Funds	APPROVE
3	Military Department Environmental Programs Increase to Meet Federal Requirements	$413,000 and four positions*	Federal Funds	APPROVE
4	Military Department Civil Support Planning Positions and Interoperable Communications Equipment	$1.0 million and four positions*	Reimbursements	APPROVE
5	CalEMA Homeland Security Training and Exercise Program	$5.1 million and 33 three-year limited-term positions	Reimbursements	APPROVE
6	Quality Assurance Representatives	$393,000 and four positions*	Federal Funds	APPROVE

**All positions are absorbed from within the Military Department's existing budget; therefore, no net increase in positions will result from these requests.*

Vote: All vote-only items approved by a 3-0 vote.

The Administration requested to withdraw BCP No. 9 in the Military's Budget; the Subcommittee voted 2-0 (Senator La Malfa absent) to deny the request and allow it to be withdrawn per the Administration's request.

Issues Proposed for Vote Only – Issue Descriptions

8940 MILITARY DEPARTMENT

For overview and budget information regarding this department, please see page 15 of this agenda.

Issue 1 – Custodian for Dublin Readiness Center and Field Maintenance Shop

Governor's Budget Request. The Governor requests increased expenditure authority of $67,000 ($17,000 GF and $50,000 federal funds) for a custodian to support the new Dublin Readiness Center and Field Maintenance Shop located at Parks Reserve Forces Training Area.

Background. The Military Department's state and federal mission require fully functional armories and maintenance facilities to meet readiness, support its full-time workforce, and provide emergency community support. The Dublin Readiness Center is scheduled for completion by May 2011; the Field Maintenance Shop was completed in December 2008. The federal government provided 100 percent of the construction funds for the Dublin facilities. The state's responsibility is to ensure the facilities are operational and maintained to meet mission requirements. The one custodian position required for this request will be absorbed from within the Military Department. The $17,000 GF used for this position will come from the armory maintenance program, which currently funds a combination of maintenance personnel and maintenance work.

Issue 2 – State Active Duty Employee Compensation Increase

Governor's Budget Request. The Governor requests a baseline augmentation of $1.363 million ($705,000 GF and $658,000 Federal Trust Fund) to cover the State Active Duty (SAD) compensation increases to be granted effective January 1, 2011, and estimated to be granted January 2, 2012.

Staff Comment. Per state statute, pay for SAD employees must be based upon military pay increases granted by Congress; additional compensation adjustments are also mandated due to a congressionally-approved increase in the military allowance for housing and subsistence. The 2011-12 estimates are 1.9 percent for salary and 1.5 percent basic allocation for housing.

Issue 3 – Military Department Environmental Programs Increase to Meet Federal Requirements

Governor's Budget Request. The Governor requests increased expenditure authority of $413,000 (federal funds) and four positions to support increasing environmental requirements within the Environmental Program Directorate.

Background. The California Army National Guard has numerous facilities throughout the state, including three major training bases covering over 50,000 acres; an aviation repair depot servicing military helicopters from 13 western states; three aviation support facilities; two equipment storage sites for armored combat vehicles; two major vehicle and weapons maintenance centers; 34 smaller vehicle maintenance shops; supply depots; and forward operating bases. For these units to be effective, they must be in compliance with all federal, state, and local environmental laws, as well as Department of Defense Instructions and Army regulations. The four positions would come at no cost to the state as they are 100 percent federally funded by the National Guard Bureau through a Master Cooperative Agreement with the state. The four positions required for this augmentation will be absorbed from within the Department and will be responsible for making sure federal construction projects can be executed in California.

Issue 4 – Military Department Civil Support Planning Positions and Interoperable Communications Equipment

Governor's Budget Request. The Governor requests increased expenditure authority of $1.0 million (reimbursements) in support of State Homeland Security Grant Program funds for emergency planning, immediate emergency response and exercise Homeland Security planning, and procurement of emergency equipment to support the Governor's Office and the California Emergency Management Agency.

Background. This request provides the Military Department with functional staff to cover the full spectrum of Homeland Security emergency planning, exercises, and operations and is critical to executing a coordinated and rapid emergency response while maintaining Continuity of Operations and Continuity of Government plans. Of the expenditure authority requested, $635,000 will enable the Department to hire four personnel to fill required assignments in operations and plans, training and exercises, operational law, and operational logistics. These positions will be absorbed from within the Department. The remaining $383,000 will be used to purchase communications equipment to allow California National Guard forces/assets a greatly increased capability to conduct interoperable communications with civilian emergency responders.

Issue 5 – CalEMA Homeland Security Training and Exercise Program

Governor's Budget Request. The Governor requests continuation of reimbursement authority in 2011-12 of $5.1 million (reimbursements) and the re-establishment of 33 three-year limited-term positions to execute an interagency agreement between the Military Department and the California Emergency Management Agency (CalEMA) for staffing support and operating expenses. The source of funds is the federally-funded Homeland Security Grant Program (HSGP).

Background. In 2003, the Military Department was assigned the responsibility of "Executive Agent" by CalEMA for all homeland security terrorism training and exercise activities funded from the various initiatives that constitute the federal HSGP. In this capacity, the CalEMA Homeland Security Training and Exercise Program (HSTEP), consisting of the Military Department and various federal, state, and local agency staff, was charged with providing statewide oversight for the training and exercise needs of California's first responder community to respond to terrorist attacks involving weapons of mass destruction. The 33 positions were originally established on a limited-term basis for purposes of the interagency agreement between the Military Department and CalEMA and all expire on June 30, 2011. These positions provide the necessary Military Department personnel to CalEMA to manage its statewide terrorism training and exercise programs for Weapons of Mass Destruction. These funds also allow for operating expenses related to the HSTEP. The proposed funding level in 2011-12 represents a reduced reimbursement level from the previous five years (from $7.5 million to $5.1 million); this is a result of a reduction in contracts for loaned executives from other governmental agencies that have been assigned to the HSTEP.

Issue 6 – Quality Assurance Representatives

Governor's Budget Request. The Governor requests increased expenditure authority of $393,000 (federal funds) for four Quality Assurance Representatives to provide on-site quality assurance and observation support to the Facilities Directorate project managers on renovation and construction projects statewide, and to help ensure that construction projects at Military Department facilities are executed in compliance with relevant building codes, specifications, and plans.

Background. The Military Department's Directorate of Facilities currently employs 14 Quality Assurance Representatives (e.g., inspectors) who provide on-site construction observation support to new construction and renovation projects at departmental readiness centers, maintenance shops, and training bases statewide. At present, a Quality Assurance Representative is typically responsible for between two and four concurrent projects, requiring each Representative to split his time between work sites. As a result, at least some work at each project site is completed un-observed by a Representative. Federal Corps of Engineers standards require that a Quality Assurance Representative be on site whenever work is being performed. The resources in this request, which are 100 percent federally-funded, will ensure federal inspection standards are met. These four positions will be absorbed from within the Department.

8860 DEPARTMENT OF FINANCE, CALIFORNIA RECOVERY TASK FORCE

Overview. On February 17, 2009, President Obama signed the American Recovery and Reinvestment Act (ARRA), a $787 billion federally-funded economic stimulus plan for a wide range of federal, state, and local programs as well as tax relief for qualified businesses and individuals. ARRA also created new requirements for state-level oversight and reporting of stimulus dollars provided to state entities.

Both the 2009-10 and 2010-11 budgets provided funding for California's ARRA accountability framework, comprised of four organizational components: the California Recovery Task Force (CRTF); the ARRA Inspector General (ARRA IG); the Bureau of State Audits (BSA); and, the State Controller's Office (SCO). Both the BSA and SCO were pre-existing entities, while the CRTF and ARRA IG were established via Executive Order by the Governor in Spring 2009.

In January 2011, Governor Brown announced he was eliminating the ARRA IG's Office six months early (funding for that office in the 2010-11 budget was provided on a one-year limited-term basis). Any outstanding audit activities of that office were transferred to the SCO or BSA.

Issue Proposed for Discussion / Vote:

Issue 1 – California Recovery Task Force – ARRA Funds Oversight

Governor's Budget Request. The Governor requests one-time funds totaling $1.6 million ($928,000 GF and $700,000 Central Service Cost Recovery Fund) to support oversight and reporting for remaining ARRA funds in 2011-12. In addition to supporting the California Recovery Task Force (CRTF), the resources in this request will also provide funding for the California Technology Agency (CaTA) and support staff at Department of Finance [Office of State Audits and Evaluations (OSAE) and Fiscal Systems Consulting Unit (FSCU)], providing information technology activities related to federally-required quarterly reports and continued audit support, respectively. Figure 1 below illustrates funding levels for the three entities comprising the CRTF generally:

Figure 1

	2010-11	**2011-12 Funding**
California Recovery Task Force	$1,700,000	$578,000
California Technology Agency	$1,400,000	$600,000
Department of Finance: (1) Office of State Audits and Evaluations; and, (2) Fiscal Systems Consulting Unit	$905,000	$450,000
TOTAL	**$4,005,000**	**$1,628,000**

**Note, the fund split is 57 percent GF and 43 percent Central Service Cost Recovery Fund.*

Background. The primary functions that remain in 2011-12 will be quarterly reporting, compliance monitoring, and ensuring that all deadlines related to retaining ARRA funds are met to avoid losing any money awarded due to failure to spend funds within the required timeframes or for other non-compliance issues. CRTF responsibilities diminish as funds are expended; therefore, this proposal significantly reduces the staffing of the CRTF to oversee the remaining ARRA funds and to provide continued quarterly reports. In September 2010, 1,121 ARRA grants remained; in 2011-12, that number will drop to 568 grants.

The CaTA is responsible for ongoing maintenance of the California ARRA and Accountability Tool (CAAT), the state's centralized reporting database. The CAAT tool provides a vehicle for departments to submit and report the data, but is only one component of the information technology (IT) required to report the information to the federal government and citizens of the state. In 2011-12, the CaTA will transition from contract/consultant staff on the CAAT system to utilization of state staff. The State IT staff will fully support and maintain the IT infrastructure (hardware, software, and connectivity), the multitude of user accounts, and provide end-user support for the ongoing reporting. Currently, there are over 300 registered users uploading over 1,100 reports consisting of thousands of records to the system in multiple formats. There will be savings realized in 2011-12 as the maintenance and support is transitioned from contractor resources to state staff, however CAAT requires continuous support and maintenance due to the complexity of the system and the continued reporting to the federal government. The funding for position support will be absorbed within the CaTA.

Staff Comment. The proposed resources for the CRTF in 2011-12 have been reduced from the level provided in 2010-11 reflective of the declining workload. However, staff notes that this request includes 5.1 positions for the CRTF itself and 4.9 borrowed staff from the Department of Finance. This level of staffing is still potentially excessive given that the workload now consists primarily of recipient reporting to the CAAT which is administered by the CaTA. Additionally, given that 57 percent of this request is funded by the GF, close scrutiny is warranted to ensure that the staffing resources provided match the workload.

Staff Recommendation: Hold open pending receipt of additional workload information.

Vote: Request held open.

1700 DEPARTMENT OF FAIR EMPLOYMENT AND HOUSING
1760 DEPARTMENT OF GENERAL SERVICES

Department Overview. The Department of Fair Employment and Housing (DFEH) is responsible for protecting the people of California from unlawful discrimination in employment, housing, and public accommodations, and from the perpetration of acts of hate violence. The Department's jurisdiction extends to individuals, private or public entities, housing providers, and business establishments within the State of California.

Budget Overview. The January Governor's Budget provides the DFEH with 197 authorized positions and $21.7 million ($16.2 million GF).

In 2010-11, the DFEH consisted of 207 authorized positions, including ten positions (eight positions in headquarters including the Chief Information Officer, one position in southern California, and one position in the Bay Area) which were used to provide information technology (IT) services for the department and 150 positions in the department's enforcement division. Three of the IT positions were eliminated as part of the DFEH's workforce cap reduction, leaving seven remaining authorized positions to support IT workload.

Issue Proposed for Discussion / Vote:

Issue 1 – Information Technology Transfer to Department of General Services; Retain Two Positions for Enforcement

Governor's Budget Request. The Governor requests to permanently transfer DFEH's Information Technology (IT) function and five positions to the Department of General Services (DGS) and proposes budget provisional language that sets aside $507,000 GF from DFEH to pay for the transferred functions. In addition, the Governor proposes to redirect the two remaining IT positions to DFEH's enforcement division on a two-year limited-term basis to process claims resulting from the settlement of a class-action lawsuit.

Background. The DFEH entered into an agreement with the DGS effective July 2010 which transferred DFEH's entire IT function and five positions to DGS's IT unit and provided $465,000 to DGS for the cost of providing these services in 2010-11. One objective of this agreement was to achieve efficiency and cost savings.

In September 2010, DFEH reached its first multi-million dollar discrimination settlement, totaling more than $6.9 million. According to the DFEH, the settlement will result in a significant increase in workload. The DFEH, therefore, is proposing to retain the two remaining IT positions and convert them into two-year limited-term positions in its Special Investigations Unit to address expected new workload stemming from the settlement of 1,500 family leave claims. All claims are required to be submitted by February 15, 2011. Shortly thereafter, the designated third-party administrator will submit all timely and valid claim forms to DFEH and DFEH staff will then conduct an independent evaluation of each claim to determine whether, on a case-by-case basis, the claimant experienced a California Family Rights Act violation and, if so the type of violation and the appropriate level of damages.

LAO Comment. Centralizing the DFEH's IT function within DGS is reasonable. However, transferring the five positions from DFEH to DGS without having DGS justify the need for these additional staff reduces transparency may not accurately reflect the new workload. If DGS is unable to absorb the increased workload, then it can request the appropriate level of additional staff and provide workload justification.

The DFEH is also requesting to redirect two positions from its former IT unit to its enforcement division to handle the workload related to the settlement of the class-action lawsuit. At the time this request was prepared, the volume of claims that would need to be processed was unknown. The DFEH indicates that it will know the total number of settlement claims filed by mid-February and be able to better describe its workload needs then. In addition, given that pursuing large class action settlements, rather than individual claims, is a relatively new effort for the DFEH, the LAO continues to examine this request. The LAO has also raised questions to DFEH about which party should be responsible for paying the related administrative costs when administering a large settlement.

LAO Recommendation. We recommend the Legislature adopt the Governor's 2011-12 January budget proposal to transfer the DFEH's IT workload to the DGS. However, the Legislature should reject the transfer of five positions to DGS and $507,000 GF to pay for these staff. Instead, the LAO recommends elimination of the five positions at DFEH and that the Legislature require DGS to justify the need for additional staff on a workload basis. Should DGS incur additional costs, DFEH should provide the appropriate level of reimbursements to fund this workload. In addition, the LAO recommends the Legislature withhold approval of redirecting two positions from DFEH's IT unit to its enforcement division until the volume of the new workload is better known. The LAO continues to examine what would be the most appropriate source of funding for this workload.

Staff Comment. Staff concurs with the LAO assessment that workload justifications are necessary before the Legislature can approve the request for: (1) DFEH to retain two positions for enforcement; and (2) DFEH to provide reimbursement to DGS for the cost of DGS providing IT functions to DFEH. Otherwise, the resources provided, particularly with regard to the reimbursement between DFEH and DGS, could be greater than is warranted. This is particularly important if the Administration is considering transferring IT workload from other small departments to DGS. Establishing a precedent here where inefficiencies are imbedded in the reimbursement level should be avoided. Additionally, it is worth noting that DFEH is 75 percent funded by the GF.

Staff Recommendation. Staff recommends the following:

1. Approve the transfer of the DFEH IT function and workload to DGS;
2. Sweep the excess five positions at DGS that could be redirected to the transferred DFEH function as well as the $300,000 Service Revolving Fund; and,
3. Hold open the: (a) DFEH request to retain the two positions, and (b) DFEH providing reimbursement to DGS for the transferred IT function; consider both of these aspects of the request at the Subcommittee's February 10, 2011, "open issues" hearing, after both DGS and DFEH submit workload justifications supporting the transferred IT function and additional enforcement activities, respectively.

Vote: Staff recommendation approved on a 3-0 vote.

1760 DEPARTMENT OF GENERAL SERVICES

Department Overview. The Department of General Services (DGS) provides management review and support services to state departments. The DGS is responsible for the planning, acquisition, design, construction, maintenance, and operation of the state's office space and properties. It is also responsible for the procurement of materials, data processing services, communication, transportation, printing, and security.

Budget Overview. The January Governor's Budget provides the DGS with 3,923.8 authorized positions and $1.1 billion ($5.5 million GF). This is a decrease of eight positions and $18.5 million. As a central service agency, the vast majority of DGS' budget is comprised of special fund and reimbursement revenue, received for services performed for other state departments and agencies.

Issue Proposed for Discussion / Vote:

Issue 1 – Office of Public School Construction, Emergency Repair Program

Governor's Budget Request. The Governor proposes a state operations reduction of $247,000 GF and 1.9 positions for the Office of Public School Construction (OPSC) administration of the Emergency Repair Program (ERP) in 2011-12. This request will conform OPSC budget resources to the remaining workload needs of the ERP.

Background. As a part of the *Williams vs. State of California* settlement [Chapter 899, Statutes of 2004 (SB 6)], the ERP was established to provide a total of $800 million for the purpose of addressing emergency facilities needs at school sites in deciles 1 through 3. To date, the OPSC has processed approximately $510 million in applications, of which approximately $338 million Proposition 98 GF has received funding. The OPSC has received applications from eligible school districts at a level that, once processed and funded, will fulfill the State's obligations pursuant to the terms of the *Williams* settlement. More specifically, the OPSC will require 2.9 PYs and $280,000 in 2010-11, and 1.0 PYs and $93,000 in 2011-12, to process the approximately $290 million remaining applications. No workload will remain for the ERP once applications are processed up to the $800 million funding level specified in the *Williams* settlement.

Staff Comment. Staff notes no issue with the content of this request; it is consistent with a recent vote of the State Allocation Board (SAB), which directs the work of the OPSC, to stop accepting ERP applications due to the program reaching its expenditure level. However, staff notes that on process this request fails to meet a clear directive provided by this Subcommittee last year when, considering several OPSC requests, it clearly stated that future OPSC budget requests needed to be reviewed by the SAB per Education Code Section 17070.65 and prior to their being included in the Governor's budget. In approving this state operations reduction, the Subcommittee may wish to again restate its concern that the Administration is not consulting with the SAB regarding the OPSC's budget.

Staff Recommendation: Approve the state operations budget reduction.

Vote: State operations budget reduction approved on a 3-0 vote.

2240 DEPARTMENT OF HOUSING AND COMMUNITY DEVELOPMENT

Department Overview. A primary objective of the Department of Housing and Community Development (HCD) is to expand housing opportunities for all Californians. The Department administers housing finance, economic development, and rehabilitation programs with emphasis on meeting the shelter needs of low-income persons and families, and other special needs groups. It also administers and implements building codes, manages mobilehome registration and titling, and enforces construction standards for mobilehomes.

Budget Overview. The January Governor's Budget provides the HCD 598.6 authorized positions and $256.0 million ($8.8 million GF). This is a decrease of 6.5 positions and $490.0 million.

The majority of the HCD's expenditures are supported by general obligation bond revenue. The budget includes no bond appropriation authority in 2011-12 (discussed as Issue 2 below). Even without this appropriation, HCD's budget has been steadily decreasing in recent years due to the pending exhaustion of housing bond funds.

Issues Proposed for Discussion / Vote:

Issue 1 – Community Development Block Grant Service Funding Adjustment

Governor's Budget Request. The Governor requests a shift of $1.1 million in federal budget authority from State Operations to Local Assistance and a reduction of ten positions for the Community Development Block Grant (CDBG) program to reflect a correction in federally allowable administrative costs. To accommodate the reduced level of program administration funding, HCD plans to: (1) reduce the number of awards for the Planning and Technical Assistance and Enterprise Fund Categories of the CDBG program; and, (2) decrease the number of awards in the CDBG General portion of the program by increasing the average award.

Background. HCD's CDBG program was created over twenty-eight years ago to address the fact that California's non-entitlement jurisdictions, which are smaller communities (many of which are rural and economically distressed), lack the resources and/or economies of scale to receive, award, and monitor these federal grants in an efficient and effective manner that allocates the funds to the most pressing needs, meets all federal requirements, and protects against fraud. Presently, HCD's CDBG program serves 168 non-entitlement jurisdictions. By consolidating the administration of the CDBG program for these communities into HCD, the state gains substantial economies of scale and program effectiveness, reducing the number of staff that need to be trained, and gaining the ability to target the most pressing needs across all of the eligible communities.

Although HCD has authority for 28 positions, the federal funds available to the department is only sufficient to support 18 of those positions. The source of the current problem is a combination of short- and long-term factors and some recent issues regarding the funding for the HCD administration of the CDBG program, including: (1) the complexity and scope of the Program makes it labor intensive to administer; (2) the federal allowance for State administration costs for the Program is minimal; and, (3) the $1.1 million increase in the Program budget in 2007-08, which included a shift of $697,000 CDBG program administration funding from GF to federal funds, cannot be sustained due to federal restrictions.

In order to absorb the 30 percent decrease in support dollars, HCD developed the following solution to maintain a viable program at the new program administration funding level:

Workload Driver	Historical Program Level	Proposed Program Level 2011-12	% Change in Activity
Notices of Funding Ability (NOFAs) Offered	6	1	(-) 83.3%
Eligible Activities Offered	81	1	0%
Volume of Awards	112	39	(-) 65.2%
Volume of Activities Requiring Field Monitoring	158	59	(-) 62.7%
Actual Monitoring Site Visits to be Completed	44	20	(-) 54.5%
Jurisdictions Served	66	39	(-) 40.9%

Staff Comment. While the amount of dollars represented in this request are insignificant in comparison to the total funding awarded to non-entitlement communities annually ($1.1 million against an average annual award total of $37 million), it could be argued that the program administration changes the HCD proposes are significant. Administering these funds in one NOFA instead of six per year, restricting eligibility to those jurisdictions that do not have an open grant or have an open grant and have met a 50 percent expenditure requirement, and increasing the award size (which will reduce the overall number of awards) will impact the rural communities that rely on HCD for their CDBG funds. As such, the Subcommittee may wish to defer action on this request to allow time for the impacts of these proposed changes to be fully analyzed and determine if there are other approaches that could be developed that would have less programmatic impact on recipient communities.

Staff Recommendation: Deny the budget request without prejudice; consider during the Spring 2011 budget process.

Vote: Request denied without prejudice on a 3-0 vote; Subcommittee will consider during the 2011 budget process.

Issue 2 – 2011-12 Housing Bond Appropriation Authority

Governor's Budget Request. The Governor proposes a one-time pause in the issuance of state bonds for new loans and grants for general obligation bond funded projects. This proposal would not affect projects that are already underway, but would impact new loans and grants by potentially delaying them for four to five months. The Administration is proposing this pause to allow time for further analysis of bond sales, the state's overall bonding capacity and debt service obligations, as well as to prioritize allocation of bond resources. This pause will also save an estimated $248 million in GF interest costs.

With regard to HCD, the Governor further proposes that $99 million in new loans and grants for housing projects, which would otherwise be administered by HCD in 2011-12, be suspended independent of any bond sale in 2011-12.

2010-11 Budget. The 2010-11 Budget included several appropriations of Proposition 1C Housing and Emergency Shelter Trust Fund Act of 2006 funds, including: (1) $25 million for the Housing Related Parks Program; (2) $5 million for the Building Equity and Growth in Neighborhoods Program; and (3) $9.275 million in remaining Infill Incentive Grant Program funds.

Background. The Department of Finance indicates that the current General Obligation bond cash balance is sufficient to fund: (1) ongoing projects through December 2011; and (2) new allocations through June 2011 and subsequent cash needs through December 2011. This ensures that no existing bond-funded project will be delayed by the proposed pause in the spring bond sale.

For every other department except HCD, new project allocations in the July through September 2011 period may be delayed for four to five months until the fall bond sale is complete. In the case of HCD, the administration has instead proposed to suspend new loans and grants for housing projects in 2011-12. This would affect programs such as Transit Oriented Development and Housing Related Parks, both of which have a remaining fund balance awaiting appropriation.

Staff Comment. While the pause in the spring bond sale could cause a delay in the jobs/economic development benefit of bond-funded projects being green-lighted, most departments have more bond proceeds than they can spend. As of December 2010, the State Treasurer estimated that the state had about $13 billion in bond proceeds that still had not been spent. So the state would still be spending down that balance and contributing to the economy over the next year even without the spring sale.

Staff notes that the Administration's proposal to suspend HCD housing bond grants in 2011-12 presents a policy question for the Legislature. The net effect of the Administration's proposal is to say that, when the bond sales resume in the fall of 2011, housing grants present no priority for new bond proceeds in 2011-12. Given this, the Subcommittee may wish to act to ensure that housing bonds are given an equal ability to be prioritized and allocated in 2011-12.

Staff Recommendation: Remove Item 2240-401 from the budget bill and adopt placeholder replacement language to authorize HCD to award housing bond funds in 2011-12.

Vote: Staff recommendation approved 2-1; Senator La Malfa voting no.

8940 MILITARY DEPARTMENT

Department Overview. The California Military Department (CMD) is responsible for the command, leadership, and management of the California Army and Air National Guard and five other related programs. The purpose of the California National Guard (CNG) is to provide military service supporting this state and the nation. The three missions of the CNG are to provide: (1) mission ready forces to the federal government as directed by the President; (2) emergency public safety support to civil authorities as directed by the Governor; and (3) support to the community as approved by proper authorities. The CMD is organized in accordance with federal Departments of the Army and Air Force staffing patterns. In addition to the funding that flows through the State Treasury, the CMD also receives Federal Funding directly from the Department of Defense.

Budget Overview. The January Governor's Budget provides the CMD with 854.5 authorized positions and $144.3 million ($46.0 million GF). This is a decrease of 11.0 positions and an increase of $3.8 million ($1.1 million GF).

Issue Proposed for Discussion / Vote:

Issue 1 – California National Guard Behavioral Health Outreach Liaison Program

Governor's Budget Request. The Governor requests continuation of the California National Guard Behavioral Health Outreach Liaison (BHOL) Program and the three existing positions, funded by $451,000 in Proposition 63 funds.

Background. The BHOL program was authorized in 2009-10 as a pilot program. The BHOL program consists of two licensed clinical staff members and one agency coordinator. These personnel ensure that appropriate mental health information is available for all California National Guard members returning from military deployment. Program staff are responsible for providing training for county and other mental health agency entities throughout California. In addition, BHOL teams coordinate directly with county veteran service officers and mental health officers and continue to integrate the behavioral health programs with the state's Operation Welcome Home program.

Staff Comment. Staff concurs that BHOL is a meritorious program, serving a unique population of National Guard members returning from deployment. These citizen-soldiers are immediately reintegrated back into their communities and families after experiencing posttraumatic events that often have affected the servicemembers' mental health needs. The BHOL program has been operating on a pilot basis; approval of this request would make the program and its staffing permanent within existing funding and staffing levels. Should the Subcommittee approve this request, staff recommends that reporting language be added to collect baseline program data, such as specific program offerings and number of servicemembers served.

Staff Recommendation: Approve the budget request, including reporting language.

Vote: Budget request with reporting language approved 3-0.

SUBCOMMITTEE NO. 4 Agenda

Senator Michael J. Rubio, Chair
Senator Doug La Malfa
Senator Noreen Evans

Tuesday, February 1, 2011
9:00 a.m. Room 112

Consultant: Keely Martin Bosler

State Administration and General Government

0860 State Board of Equalization

Background. The Board of Equalization (BOE) is one of California's two major tax collection and administration agencies. In terms of its responsibilities, BOE: (1) collects state and local sales and use taxes (SUT) and a variety of business and excise taxes and fees, including those levied on gasoline, diesel fuel, cigarettes, and hazardous waste; (2) is responsible for allocating certain tax proceeds to local jurisdictions; (3) oversees the administration of the property tax by county assessors; and (4) assesses certain utilities and railroad property. The board is also the final administrative appellate body for personal income and corporation taxes, which the Franchise Tax Board (FTB) administers. The BOE is governed by a constitutionally established board—consisting of four members elected by geographic district and the State Controller.

Governor's Budget. The *2011-12 Governor's Budget* proposes **$496 million** in support of BOE operations, of which **$283 million is General Fund**. The remaining budget consists mainly of reimbursements from local governments and support from various special funds. The proposed level of support represents a net increase of $13 million General Fund mainly from a budget proposal to continue a Statewide Compliance and Outreach Program that has been generating approximately $40 million annually from increased taxpayer education, outreach, and audit activities.

The number of personnel-years (PYs) for BOE is budgeted to increase slightly from 4,470 to 4,485.

Tax Gap Reduction Measures

Background. The BOE estimates that the total tax gap for all its programs is about **$1.5 billion**. The tax gap is defined as the total tax receipts due to the state less the tax receipts collected by BOE. The tax gap for the sales and use tax, the board's largest tax program, represents the majority of the tax gap.

The department has undertaken several initiatives to reduce this tax gap. However, a reduction to the Board's budget in 2009 and subsequent hard hiring freezes to manage this reduction has resulted in many vacancies at the board and has slowed the board's efforts to reduce the tax gap. The BOE estimates that it has an additional 180 vacancies they are trying to fill. Furthermore, the majority of the BOE's workforce is SEIU 1000 – whose contract signed last fall continued a personal leave program of one-day a month for a year. This has also temporarily reduced the personnel hours available to close the tax gap and the board has estimated it will cost the state $45 million General Fund in lost revenue collections in the current and budget years.

Question.

- **BOE.** Please explain what actions you have taken to reduce the revenue loss from the current hiring freeze and the PLP contract provisions?

1. Statewide Compliance and Outreach Program

Background. The BOE was approved to implement a three year pilot called the Statewide Compliance and Outreach Program (SCOP) in 2008. This program supported 148 new positions to focus on identifying and registering entities actively engaged in business in California whom were selling tangible personal property without a seller's permit. Seven teams were created across the state to perform permit checks. As of June 30, 2010, the SCOP had visited over 146,000 retail businesses and identified over 3,300 businesses operating without a valid seller's permit. Nearly 95 percent of businesses visited that did not have a seller's permit, voluntarily obtained the permit after the SCOP's visit. Noncompliant businesses were referred internally to the BOE's Legal Department, Investigations Division and then ultimately to local District Attorney's for prosecution.

The BOE estimates that the education and outreach activities of the SCOP have significantly increased voluntary compliance and has resulted in reducing the tax gap by approximately $68 million, annually. The BOE estimates that the benefit to cost ratio of this program is 4.8:1. Furthermore, the SCOP has also worked cooperatively with local governments to provide referrals concerning businesses operating without valid city/county business licenses.

Governor's Budget. The Governor's budget proposes to continue the SCOP program for an additional two years. The Governor's budget would extend the 147 positions for an additional two years at a cost of **$14.2 million** ($10.2 million General Fund).

Additional Businesses Required to Register…Means More Compliance Work to Do. A law change in 2009 (ABx4 18, Budget) required non-retail businesses with receipts of more than

$100,000 to register with the BOE and file annual use tax returns by April 15 each year. The annual use tax return and payment applies to purchases on which sales tax was not collected (generally from out-of-state sellers). This has resulted in BOE registering approximately 300,000 additional businesses (in addition to 197,000 retail businesses that already had seller's permits).

Given the recent law change described above to increase use tax compliance, there is likely significant education and outreach that is needed to ensure compliance with the new law.

Question.

- **BOE:** What are you doing to ensure that the new non-retail businesses are in compliance with use tax filing rules?

Staff Recommendation. Staff recommends that the Subcommittee approve this budget proposal on a permanent basis, but require annual reporting to ensure efficacy of the program over time.

2. Use Tax Collection - Voluntary Disclosure Program

Background. One component of the tax gap are the sales and use tax liabilities of businesses and individual consumers on products purchased from out-of-state vendors not required to collect the use tax. The use tax voluntary disclosure program was initiated in 2003 and extended permanently in 2010 (SB 858, Budget). This program places a line item on the income tax form for taxpayers to self report use tax that was not paid on items purchased from out-of-state vendors.

The BOE has indicated that this policy has resulted in an estimated **$10 million** in state and local revenue annually. The cost of this program is approximately $100,000.

Legislation, AB 469 (Eng), vetoed by the Governor in 2009, also contained other provisions that other states have used to improve voluntary use tax collections. These provisions include providing a "look-up" table to assist taxpayers in calculating their tax liability, and a mandatory reporting requirement if the tax was not reported to BOE. The BOE estimates that a look-up table could generate approximately $10.6 million ($6.5 million General Fund) in additional revenues by increasing use tax collections.

Staff Comments. Staff finds that the existing voluntary reporting mechanism for use tax that has not been paid has helped to close the tax gap at relatively little cost to the state. Additional progress could be made on closing the tax gap by providing a "look-up" table to assist taxpayers in complying with current law related to the use tax.

Staff Recommendation. Staff recommends that the Subcommittee adopt trailer bill language to do the following:

- Direct BOE to develop a "look-up" table to assist taxpayers in compliance with current law.

3. Sales Tax Nexus

Background. Under current law, purchases of tangible personal property are subject to use tax when purchased from any retailer even when purchased on the Internet. Current law also specifies that retailers that are considered to be engaged in business in California are required to collect use tax at the point of purchase by California consumers. However, a growing tax gap has emerged with Internet retailers that do not claim to be engaged in California technically and do not collect use tax on purchases made by California consumers. This has disadvantaged small business and corporations that do maintain brick and mortar presence in California.

The BOE has estimated that this law change would generate approximately **$100 million** right away, but there is significant potential for this number to grow.

Other States Have Acted to Close this Tax Gap. New York has closed this tax gap by redefining a "retailer engaged in business in this state" to include any retailer with an agreement with a resident that directly or indirectly refers business to the Internet retailer. This is commonly referred to as the "affiliate nexus" approach to closing the tax gap. In the case of New York state, Amazon.com challenged this law in court, but the Internet retailers started collecting the tax on purchases made by New York consumers immediately and continue to do so. The first court ruled in favor of New York state and the case is currently on appeal.

It is also important to note that Amazon.com did not pull the contracts with its affiliates, which has been a common concern when discussing this approach to closing the tax gap. Many other states have been considering a similar approach and in 2010 the Senate passed ABx8 8 (Budget) that was ultimately not passed by the Assembly. This "affiliate nexus" approach to closing the tax gap is being pursued in AB 153 (Skinner) in the current legislative session.

Corporations Benefit from Income Tax Cuts, but Do Not Claim Nexus. In 2008 the Legislature passed a new corporate tax cut that allows corporations that accumulate business tax credits to assign all or a portion of the unused credit to an affiliated corporation that is the member of the same combined reporting group. However, while these corporations may claim nexus for corporation tax purposes they may not claim nexus for sales tax purposes. Therefore, the recent credit sharing law that was passed in 2008 can benefit companies that do not claim nexus for sales tax purposes.

One example of a corporate structure described above includes Lab 126 located in Cupertino, California, which developed the Kindle e-reader. The Lab's parent company Amazon.com does not claim nexus in California for the purposes of collecting sales tax.

Legislation has been introduced in the Assembly (AB 155, Calderon) this year that would provide that a retailer whose parent has corporation tax nexus and whose subsidiaries in the state perform activities related to its retail efforts also have sales tax nexus.

Staff Comments. Current law has set up a comparative disadvantage for firms with brick and mortar invested here in California. Given the rise of Internet shopping, this is likely one of the areas where the tax gap has continued to widen. Furthermore, the development of Internet shopping tools such as Google Shopping allows consumers to identify which websites do not collect tax. This contributes to further confusing consumers in to thinking that use tax is not owed on purchases made on the Internet.

Staff Recommendation. Staff recommends that the Subcommittee hold this issue open, but consider adopting trailer bill to close the tax gap related to Internet purchases by:

(1) requiring Internet retailers with affiliate nexus to collect sales tax on behalf of California consumers; and

(2) requiring that certain Internet retailers that have corporation tax nexus also have sales tax nexus.

Other Issues

1. Headquarters Building

Background. The BOE Headquarters Building has a long and expensive history of problems. Construction was completed in 1993. The building has been fraught with construction defects causing water leakage, mold, and falling glass. The building has also experienced major system failures, including plumbing and the elevators. A major project was completed in 2006 to help remedy the problems. However, other problems continue and numerous employee complaints and lawsuits have ensued. The BOE estimates that this loss in productivity has resulted in annual revenue loss of approximately $22 million.

Furthermore, the BOE Headquarters building does not adequately meet BOE's space needs. Presently, the BOE staff is spread out over five different locations and the BOE has approximately 700 more positions than capacity at the main headquarters building.

The State started the process of purchasing the building from CalPERS several years ago. The State Pooled Money Investment Board (PMIB) advanced BOE around $91 million from the PMIB to purchase the building from CalPERS. The PMIB then would be repaid with the proceeds of a lease revenue bond sale. On November 15, 2010, the State Public Works Board authorized the sale of lease revenue bonds to repay the PMIB loan. The BOE estimates that the annual rent on the headquarters building will increase to nearly $13 million annually. This is an increase of approximately $2 million ($1.1 million General Fund) annually starting in 2011-12 to cover the full debt service costs of the bonds.

Governor's Budget. The Governor's budget includes an augmentation of **$2.1 million** ($1.1 million General Fund) to cover projected rent increases to cover the full debt service costs as projected by BOE.

Staff Recommendation. Staff recommends that the Subcommittee reject this budget proposal without prejudice. This issue can be considered later this session if additional information is presented.

2. Dell Computer Settlement

Background. The BOE has been named as the cross defendant in the class action case of *Diane Mohan v. Dell*. This case is currently pending in San Francisco County Superior Court. The case involves the collection of use tax by Dell Computers on the extended warranty service contracts during the years 2000 to 2008. The extended warranty service contract is an intangible and the court found that the use tax was collected erroneously. The class action attorneys have estimated as many as 10 million transactions over this time period. The BOE's experience is that about 20 percent actually completed refund claims and submitted them for payment, but this could still mean hundreds of thousands of claims that need to be processed.

The BOE has indicated that it does not have the staff to process these additional transactions. However, to date no final determinations or orders have been issued by the court about who will pay for these transactions.

Governor's Budget. The Governor's budget includes a "placeholder" request of **$4.2 million** ($2.8 million General Fund) in the budget year and $1.6 million ($1.1 million General Fund) in 2012-13 and 2013-14 to support 8 three-year limited term positions to address the additional workload associated with processing the Dell refunds.

Staff Recommendation. Staff recommends that the Subcommittee reject this budget proposal without prejudice. This issue can be considered later this session if additional information is presented.

1730 Franchise Tax Board

Background. The Franchise Tax Board (FTB) is one of the state's two major tax collection agencies. The FTB's primary responsibility is to administer corporation tax programs and California's personal income tax (PIT). In addition, FTB administers several non–tax–related programs, including the collection of child support payments and other court–ordered payments. The FTB is governed by a three–member board, consisting of the Director of Finance, the Chair of the Board of Equalization (BOE), and the State Controller. An executive officer, appointed by the board, administers the daily operations and functions of FTB.

The *2011-12 Governor's Budget* proposes **$586.5 million** in support of FTB's operations, of which **$551 million is General Fund**. The remaining budget consists mainly of other special funds related to FTB's court collection and Department of Motor Vehicles collection programs. The proposed level of support represents a net increase of almost $9 million General Fund mainly from budget proposals to augment the FTB's audit program and provide upgrades to FTB's mainframe computer system.

The number of personnel-years (PYs) for FTB is budgeted to decline slightly from 5,434 to 5,260.

Tax Gap Reduction Measures

Summary. The FTB estimates that its total tax gap is about **$6.5 billion**. The tax gap is defined as the total tax receipts due to the state less the tax receipts collected by FTB. The department has undertaken several initiatives over the last six years to reduce this tax gap using an enterprise approach. An enterprise approach means that staffs from all different divisions at FTB are involved in reducing the tax gap, including filing, audit, legal, and collections divisions.

The FTB has reported that it is on track to raise the additional revenues ($114 million) related to recent tax gap enforcement efforts, including the augmentations made last year to continue the board's ability to mine the DMV luxury auto registrations and IRS Information Return Master File for tax noncompliance leads and fund a vendor contract to identify good mailing addresses.

Recent efforts to reduce the tax gap have been negatively impacted by furloughs, hiring freezes, and the Personal Leave Policy (PLP) negotiated as part of the SEIU 1000 contract. The FTB has indicated that it did try and minimize the impacts of the furloughs by reducing non-revenue generating activities and low-return activities. However, regardless, the FTB estimated that 1.5 million hours were lost due to the furloughs and the more recent hiring freeze and PLP have further reduced revenues.

Question.

- **FTB.** Please explain what steps you have taken to minimize the revenue losses associated with the current hiring freeze and PLP contract provisions?

1. Audit Workload

Background. The FTB's audit program is responsible for conducting examinations of taxpayer income tax returns and claims for refunds in order to determine whether the self-assessed tax liabilities were calculated correctly. Historically, the audit program has prioritized audit models and processes have been evaluated based on the workload benefits (revenue) to costs and has pursued audits that return at least $4 of benefit to every $1 of cost invested in the audit.

The FTB recently assessed its audit workload and identified that there was additional capacity for audit staff that would generate at least a 4:1 cost benefit ratio.

Governor's Budget. The Governor's budget includes a proposal to add 34 positions at a cost of **$3.2 million** General Fund to augment the FTB's audit program. The FTB estimates that these additional auditors would generate **$13 million in additional revenues** in 2012-13 and $6.5 million in the budget year due to the time it takes to staff and train new auditors.

Staff Recommendation. Staff recommends that the Subcommittee approve this budget proposal.

2. Financial Institutions Records Match (FIRM)

Background. In recent years the FTB has pursued the implementation of a Financial Institutions Records Match (FIRM) system to help reduce the tax gap. The FIRM is an information technology project that would require financial institutions doing business in California to match FTB information on delinquent tax and non-tax debtors against their customer records on a quarterly basis. The FIRM is patterned after the FTB's Financial Institution Data Match system, which is a project implemented as a result of federal legislation to identify the assets of delinquent child support debtors.

The Senate passed legislation (ABx8 8, Budget) in 2010 to authorize FTB to implement a FIRM system. However, ultimately this legislation was not passed by the Assembly. The FTB would use the new data collection aid in the collection of debts under the authority of the existing Order to Withhold statutes. The proposal would not impact existing law that provides the applicable constitutional due process protections and appeal rights available in either the audit or collection processes. In addition, ABx8 8 required FTB to reimburse a financial institution for its actual costs incurred to implement FIRM, up to $2,500 for startup costs and no more than $250 per calendar quarter thereafter. This amendment removed bank opposition to this measure. A Feasibility Study Report (FSR) has been completed on this project.

Governor's Budget. The Governor's budget includes **$1.3 million** General Fund to support 3 positions in the budget year to start implementation of the FIRM system. The budget for this system when fully implemented would be $5.1 million to support 42 positions. The initial positions would be related to getting the technical aspects of the system functional and the additional positions in 2012-13 would support additional accounts receivable staff needed to collect funds identified by the bank record matches.

Approximately $540,000 in the budget year and $2.3 million in 2012-13 would be to reimburse the banks each quarter for their costs associated with implementing the FIRM system.

The Governor is proposing trailer bill language to implement this program – the trailer bill language is substantively the same as the language passed by the Senate in 2010.

The board has estimated that this proposal will generate **$43 million in additional revenues** in the current and budget years.

Staff Comments. Staff finds that the tax gap continues to be a burden on taxpayers that comply with all the state's tax laws. Staff finds that the FIRM system would help to reduce the tax gap by using a methodology that has been proven in the child support system.

Staff Recommendation. Staff recommends that the Subcommittee adopt the Governor's budget proposal and trailer bill language to implement the FIRM system.

3. Voluntary Compliance Initiative 2011

Background. Current federal and state law place reporting requirements and restrictions on abusive tax shelters and related transactions designed to avoid taxes. The use of and failure to report such transactions is subject to assessment, substantial penalties, and interest by the FTB up to eight years after the tax return is filed by the taxpayers.

The FTB, over the past decade, has implemented two amnesty-type efforts to recover past-due state tax revenues, a Voluntary Compliance Initiative in 2003 and a general tax amnesty program in 2005. In total these programs resulted in the collection of $4.5 billion in additional tax revenues (some of these revenues would have been collected in future years but due to the amnesty and Voluntary Compliance Initiative collection was accelerated). Under these programs, taxpayers that were already under audit or anticipating audit had an opportunity to pay the tax, pay reduced penalties, and avoid criminal prosecution associated with their tax avoidance strategies.

Governor's Budget. The Governor's budget includes a proposal to implement another Voluntary Compliance Initiative. The proposal includes **$513,000** to support 5.5 positions to backfill other revenue generating positions that would have to be redirected to implement this program. The FTB estimates that the 2011 Voluntary Compliance Initiative described in more detail below will generate approximately **$270 million in additional revenues** in the current fiscal year.

This new 2011 Voluntary Compliance Initiative would begin on August 1, 2011 and end on October 31, 2011. It would apply to taxable years before January 1, 2011. Specifically the proposal would create a narrow amnesty for certain taxpayers that have abusive tax avoidance transactions that are currently under audit, in protest, or are currently unknown to the FTB. This proposal would also apply to taxpayers with other unreported income from the use of an offshore financial arrangement.

The 2011 Voluntary Compliance Initiative would include the following incentives for businesses and individuals to participate:

- Waiver of all penalties, except the Large Corporate Understatement Penalty and Amnesty Penalty for qualified participants.
- No criminal action (amnesty) would be brought against any participant, unless they are currently the subject of a criminal complaint or under criminal investigation in connection with an abusive tax avoidance transaction.

The 2011 Voluntary compliance initiative would also make the following changes to further reduce the use of abusive tax avoidance transactions prospectively:

- Increase the statute of limitations for the FTB related to abusive tax avoidance transaction cases from eight to twelve years.
- Enact a uniform definition of abusive tax avoidance transactions.
- The abusive tax avoidance transaction use penalty would be modified to prevent taxpayers from avoiding the penalty by filing an amended return after being contacted by FTB, but prior to the FTB issuing a deficiency notice. Instead 50 percent of the penalty

would be imposed on any amended return filed after the Voluntary Compliance Initiative period.

- Amend the noneconomic substance transaction (NEST) penalty so that it is imposed on any California understatement resulting from a transaction the IRS examines and determines to lack economic substance.

In addition, participants in the 2011 Voluntary Compliance Initiative would be required to file amended returns and pay all unpaid tax and interest resulting from the abusive tax avoidance transaction. Furthermore, all tax years settled in the 2011 Voluntary Compliance Initiative would be closed to appeal rights.

Staff Comments. Given the FTB's past experiences with tax amnesty and the first Voluntary Compliance Initiative there is clearly short-term financial benefits that can be gained from implementing this sort of effort. Staff finds that the proposal also includes several ongoing law changes that would further discourage the future use of these tax avoidance strategies. This should have long-term impacts on the FTB's ability to close the tax gap that last beyond the 2011 Voluntary Compliance Initiative period.

The state's tax gap is unfair and places additional burden on compliant taxpayers. Good tax collection practices aim to reduce the tax gap and collect taxes that are due to the state.

Staff Recommendation. Staff recommends that the Subcommittee approve the budget proposal and trailer bill language to implement the 2011 Voluntary Compliance Initiative.

Other Issues

1. Mainframe Replacement

Background. Data security and reliability is critical for FTB given the volume of confidential taxpayer data it maintains. The FTB's data reliability is being threatened by outdated equipment and software that is out-of-support. The FTB is working towards implementing a major new information technology project called Enterprise to Data Revenue (EDR). Once this new system is implemented, FTB has estimated that it will generate $1 billion in additional tax collections annually. This new system will require upgrades to FTB's existing mainframe hardware. Furthermore, the current mainframe hardware is running very close to capacity making failure of the system more of a concern.

Governor's Budget. The Governor's budget includes **$4.7 million** General Fund on a one-time basis to replace the existing mainframe, storage device, and supporting software licenses.

Financing System Saves Upfront Cash. Staff finds that replacing the mainframe hardware is justified given the current lack of capacity on the existing system and the upcoming implementation of the new EDR system. However, given the State's current fiscal condition the staff recommends that FTB finance the replacement of the system over a three-year period. The FTB estimates that financing the system over three years would cost approximately $250,000 more than paying up front, but would save the state $3 million in the budget year. The FTB has offered this as the second best alternative in its budget change proposal.

Staff Recommendation. Staff recommends that the Subcommittee approve the mainframe replacement, but finance the replacement over a three year period.

Revenues

1. Maintain Existing Taxes: Realignment

Background. The 2009-10 budget passed in February 2009 included a 1 percent increase in the sales tax and a 0.5 percent increase in the vehicle license fee (VLF). These tax increases were passed for a two-year period. The increased sales tax and VLF rates would have been maintained for an additional one year and two years, respectively, if the voters had passed Proposition 1A in May 2009. However, the voters rejected Proposition 1A.

It was anticipated in 2009 that economic growth and reduced government expenditures would allow for the temporary revenues to expire without major budget implications. However, the economic recovery has been slow and the unemployment rate remains high. Furthermore, while some permanent spending reductions have been made including the elimination of adult dental care and the reduction of pension benefits for state employees, many solutions have been temporary and have resulted in a projected $25.4 billion budget deficit in 2011-12. Without corrective action a deficit of over $17 billion is projected in each of the next four fiscal years.

Governor's Budget. The Governor's budget has proposed a constitutional amendment to maintain the current sales tax and VLF rates for a five year period dedicated to local governments to support **$5.9 billion** in public safety programs that would be realigned from the state to the counties.

- **Maintain 1 percent Increase to State Sales and Use Tax.** The State Sales and Use Tax rate was increased from 5 percent to 6 percent effective April 1, 2009. The increase is set to sunset on June 30, 2011. The Governor's budget would extend the 1 percent State Sales and Use Tax for five additional years to support local public safety programs. This proposal is expected to generate $4.5 billion in the budget year.
- **Maintain 0.5 percent Increase to VLF.** The rate of the vehicle license fee (VLF) was increased from 0.65 to 1.15 percent of a vehicle's value, effective May 19, 2009 and will sunset on June 30, 2011. The increase from 0.65 to 1 percent went to benefit the General Fund and 0.15 of the increase was transferred to the Local Safety and Protection Account to fund local law enforcement programs. The Governor's budget would maintain this increase for five additional years to support local public safety programs, including the local public safety programs supported by the 0.15 raised in 2009. This proposal is expected to generate $1.4 billion in the budget year.

The Governor proposes to place the constitutional amendment on the ballot in June 2011.

VLF Historically at 2 Percent. The VLF is currently 1.15 percent and the Governor's proposal would maintain this rate for an additional five years to support local public safety programs. The VLF has historically been 2 percent of the market price of the vehicle. The LAO has found that a VLF rate of about 1 percent is appropriate and is consistent with the tax rate for other property (land). Furthermore, the VLF adjusts annually based on the depreciated value of the vehicle and is deductible on federal income tax returns.

The State Constitution already dedicates 0.65 of the VLF to local governments. The Governor's proposal would dedicate the remaining 0.5 for local public safety purposes.

Portions of Sales Tax Historically Dedicated to Local Government. The Sales and Use Tax is currently approximately 8.25 percent and can be up to 2 percent higher depending on the local jurisdiction since locals can generally levy an additional 2 percent through the transactions and use tax. Currently, the Sales and Use Tax is made up of the following components:

- 6 percent to the General Fund;
- 0.5 percent dedicated to local governments;
- 0.5 percent dedicated to local public safety services;
- 1 percent Bradley-Burns Uniform Local Sales and Use Tax with 0.25 percent dedicated to county transportation funds and 0.75 percent for city and county operations; and
- 0.25 percent dedicated to paying costs associated with the Economic Recovery Bond Act.

The Governor's budget proposal would maintain the Sales and Use Tax rate described above, but dedicate 1 percent currently going to the General Fund to local government to support realigned public safety programs. The LAO has indicated that maintaining this higher tax rate merits serious consideration given the magnitude of the State's budget deficit.

Staff Recommendation. Staff recommends that the Subcommittee hold this issue open.

2. Maintain Existing Taxes: Education

Background. The 2009-10 budget passed in February 2009 included a 0.25 percent surcharge on each personal income tax (PIT) bracket and a reduction in the dependent exemption credit from $309 to $99 for a two-year period. The surcharge and reduced dependent exemption credit would have been extended for an additional two years if the voters had passed Proposition 1A in May 2009. However the voters rejected Proposition 1A.

The LAO's fiscal forecast released in November 2010 projected that the Proposition 98 guarantee was expected to decline by $2 billion in the budget year. This decline is mainly the result of the expiration of the temporary taxes discussed above and in this issue. This decline would be on top of the significant loss of federal ARRA funds that are no longer available for school districts.

Governor's Budget. The Governor's budget has proposed a constitutional amendment maintaining the following tax rates for a five year period dedicated to education that will generate **$5.2 billion** annually.

- **Maintain 0.25 percent Surcharge.** A PIT surcharge of 0.25 percent was enacted effective in the 2009 and 2010 tax years. The Governor's budget estimates that maintaining this surcharge would generate $3.3 billion in the current and budget years.
- **Maintain Reduced Dependent Exemption Credit.** The dependent exemption credit was reduced from $309 to $99 effective in the 2009 and 2010 tax years. The Governor's budget estimates that maintaining this reduced credit will generate about $2 billion in the current and budget years.

The Governor proposes to place the constitutional amendment on the ballot in June 2011.

PIT Surcharge Regressive. The PIT rate ranges from 1.25 percent to 9.55 percent depending on income (this includes the temporary surcharge). Individuals with $46,766 or more in taxable income in 2010 pay the highest PIT rate on income earned above this amount. In addition, taxpayers with taxable income over $1 million pay an additional 1 percent surcharge, making their effective tax rate 10.55 percent in the 2009 and 2010 tax years.

Staff finds that the PIT surcharge is regressive in that it raises taxes the same amount at every income tax bracket. This means that proportionally an individual paying tax in the lowest bracket saw their rate increase by 25 percent, while an individual with $1 million in taxable income saw their rate increased less than 2.5 percent. The LAO has suggested that the Governor's proposal merits serious consideration given the State's fiscal situation.

LAO Supports Reduced Dependent Credit. The LAO has in the past recommended as a matter of policy reducing the dependent credit to make it consistent with the personal exemption credit, which is also $99.

Staff Recommendation. Staff recommends that the Subcommittee hold this issue open.

3. Corporate Tax Changes

Background. The 2008-09, 2009-10, and 2010-11 budget packages all included corporate tax changes. Generally these tax changes were a mix of short-term suspensions that provided temporary budget relief and permanent reductions that were made effective prospectively. These changes are outlined in further detail below.

Temporary Loss of Tax Benefit - $900 million per year for four years ($3.6 billion total)

- **Temporary Limit on Tax Credits.** The 2008-09 budget package temporarily limited to 50 percent the amount of business tax credits that could be used to reduce tax liability in the 2008 and 2009 tax years. This provided $1.3 billion in temporary revenue to the state. However, corporations were able to continue to carry these credits on their balance sheets.
- **Temporary Suspension of Net Operating Losses.** The 2008-09 budget package suspended net operating loss (NOL) deductions for the 2008 and 2009 tax years, except for taxpayers with net business income of less than $500,000 in either year. The 2010-11 budget package suspended NOLs for an additional two years, except for taxpayers with net business income of less than $300,000 in either year. Collectively these actions provided $2.3 billion over the four year period. However, corporations were able to continue to carry and accumulate these losses on their balance sheets.

Permanent Tax Cuts - $1.3 billion in permanent cuts ongoing starting in 2011.

- **Permanent Change Unitary Group Credit Sharing.** The 2008-09 budget package authorized corporations that accumulate business tax credits to assign all or a portion of any unused credit to an affiliated corporation that is a member of the same combined reporting group. With respect to credits earned in tax years beginning before July 1, 2008, the assignee corporation would have to have been a member of the group from at least June 30, 2008, through the year of assignment. For credits earned subsequently, the assignee corporation must be a member of the group in the year that the credit is earned through the year in which the assignment occurs. This tax policy change will result in a loss of General Fund revenues of approximately $315 million annually starting in the 2010-11 budget year.

- **Extend NOL Carry Forward Period and Allow for Carrybacks.** The 2008-09 budget package further expanded the NOL carry forward period from 10 years to 20 years for losses incurred after January 1, 2008. Furthermore, the budget package, amended in 2010, authorized NOL carry backs for losses incurred in 2013 or later tax years. The carry back provision will phase in, with 50 percent of any 2013 NOLs available for carry back, 75 percent of any 2014 NOLs, and full carry back for NOLs in subsequent years.

- **Elective Single Sales Factor.** The 2009-10 budget package created a permanent ***elective*** single sales factor for apportionment of business income across states. In contrast, prior law averaged a business's proportion of sales, property, and payroll in California (with the sales factor double-weighted) to apportion the California share of multi-state business income. Under this new tax policy, corporations can elect to allocate net income for California tax purposes under the old formula or 100 percent to sales. Businesses that proportionally have fewer sales in California relative to property and payroll will see their taxable income in California fall. This change will go into effect for the 2011 tax year. The annual losses projected from this policy change are in excess of $1 billion.

- **Cost of Performance.** The 2009-10 budget package replaced the “cost of performance” rule for corporate taxpayers with a market based rule when the elective single sales factor was enacted. Under the cost of performance rule sales of intangibles and services are assigned to California for tax purposes only if the greater cost of performance of the income producing activity occurs in California relative to other states. The market based rule would have required the sales of intangible goods and services to be used to apportion corporate income to California. The 2010-11 budget package repealed the market based rule returning the state to the old cost of performance rules for sourcing intangibles. The annual losses projected from returning to the cost of performance rule are approximately $100 million annually.

Governor’s Budget. The Governor’s budget modifies current law to make the single-sales factor multi-state corporate income apportionment method mandatory instead of elective. The Governor’s budget also proposes to return back to the market based rule for sourcing intangibles. These two changes are expected to generate **$1.4 billion** in the current and budget years.

Elective Single Sales Factor Disadvantages California Based Companies. Allowing corporations to elect the formula they apportion income for tax purposes gives a comparative advantage to out-of-state corporations that have high sales, but low property and payroll invested in California. By allowing the corporation to elect the formula it uses to calculate tax owed, the corporation can then choose the calculation that is most advantageous to their situation. Furthermore, changing to mandatory single sales factor will bring California more in line with other states. Of the 23 states that have adopted single sales factor, only three allow an election. The FTB estimates that the increased tax liability under mandatory single sales factor will generally come from out-of-state businesses that will have higher tax liabilities.

Cost of Performance Rule Advantages Out of State Companies. The “Cost of Performance” rule specifically advantages corporations headquartered outside of California. Moving to a market-based rule reduces the ability of taxpayers to manipulate their sales factor and makes the treatment of intangibles consistent with tangible goods.

Carryback Provision Duplicative. While the carryback policy does conform to federal policy, there are unique circumstances in California that make this policy problematic. Specifically, the Proposition 98 guarantee that funds K-14 education depends on year-over-year growth in General Fund revenues. However, the premise of carrybacks is that corporations can go back and amend prior tax returns to lower tax liabilities and even trigger tax returns. However, the state has no ability to change the Proposition 98 guarantee retroactively to adjust for the amendments to revenues. Secondly, the carry forward policy allowed by current law essentially gets at the same policy goal, which is to average a corporation’s tax liability over a period of time in order to encourage investments that may take multiple years to recover.

Staff Recommendation. Staff recommends that the Subcommittee hold this issue open, but consider the following tax policy changes:

- Adopt the Governor's proposal to implement mandatory single sales factor policy.
- Adopt the Governor's proposal to change to a market-based rule for sourcing intangibles and services.
- Repeal carryback provision.
- Suspend for two years the new credit sharing law.

4. Targeted Tax Expenditures: Enterprise Zones

Background. Existing law provides special tax incentives for four kinds of geographically targeted economic development areas. These areas include enterprise zones, local agency military base recovery areas (LAMBRAs), manufacturing enhancement areas (MEAs), and targeted tax areas (TTAs). The tax incentives enjoyed by businesses located in these areas include accelerated depreciation, 100 percent net operating loss carryover, wage credits, and credits for sales tax on equipment purchased for use in the zone. There are some differences among the tax incentives provided for each area, but taxpayers generally have access to each form of preferable tax treatment.

The law currently limits the number of enterprise zones (42), LAMBRAs (8), MEAs (2) and TTAs (1). The Department of Housing and Community Development has designated 42 enterprise zones and 7 LAMBRAs as of December 15, 2010.

Employers within enterprise zones are allowed to claim a tax credit of 50 percent of the wages paid to a qualified employee in the first year, 40 percent in the second year, 30 percent in the third year, 20 percent in the fourth year, and 10 percent in the fifth year, up to 150 percent of the minimum wage. Qualified employees include individuals: (1) eligible for job training programs; (1) eligible for most social welfare programs; (3) economically disadvantaged; (4) dislocated workers; (5) disabled and eligible or enrolled in a state rehabilitation plan; (6) veteran; (7) ex-offender; and (8) member of a federally recognized Indian Tribe. Furthermore, existing law also allows enterprise zones to designate targeted employment areas (TEAs) to contain census tracts where 51 percent or more of individuals are considered low or moderate income. Any hire made out of a TEA can qualify the taxpayer in the enterprise zone for the hiring tax credit and TEAs can be drawn outside the borders of the enterprise zones.

The tax expenditures related to these zones cost the state approximately **$300 million** annually.

Governor's Budget. The Governor's budget proposes to repeal the state tax benefits allowed in the four kinds of geographically targeted economic development areas described above. The proposal would eliminate all state tax benefits for both newly earned credits and deductions and for credits that had been earned in prior years, but have not been used. Local agencies would have the option of keeping their local incentives. This proposal will generate **$924 million** in the current and budget years.

Good Goal, But Not a Core State Responsibility. The enterprise zone program was formed in 1984 to help draw investment into depressed rural and urban areas. While this is a good goal, it is not a core responsibility of state government and given the state's chronic budget deficits it is important that all state spending, including tax expenditures be scrutinized.

Furthermore, the Governor has proposed a new option for local governments that want to continue to fund economic development activities. Specifically, the Governor has proposed a constitutional amendment to provide for 55 percent voter approval for limited tax increases and bonding against local revenues for economic development projects. Furthermore, the

Governor's proposal does not impact tax incentives that local governments may provide businesses in enterprise zones.

Program Not Proven Effective. In addition, the LAO and others have found that enterprise zone tax benefits have little to any impact on the creation of economic activity or employment in California. The LAO found that the program mainly seemed to shift economic activity from one zone to another within California without doing anything to grow economic activity. Furthermore, there is some evidence that benefits from the enterprise zone program go to taxpayers whose behavior has not been affected at all by the program, but instead by firms that specialize in finding businesses that could benefit from the program and offering to prepare the taxpayers tax return on a percent of benefit basis. In these cases it is clear that the taxpayer did not relocate their business because of the enterprise zone – since they had to be told of the tax benefit after they had already relocated.

Reform versus Elimination. Recently there have been significant efforts to make some reforms to the enterprise zone program. Specifically, SB 974 (Steinberg) from 2010 proposed to eliminate Targeted Employment Areas (TEAs) and stop the practice of retro-vouchering. As mentioned above, TEAs allow a taxpayer to qualify an employer for a tax credit not based on who they are, but based solely on residence within a zip code range listed on his or her employment records. Retro vouchering essentially allows taxpayers to gain tax credits for hiring decisions made in the past. Taxpayers often use the TEA criterion and the retro-vouchering to check payroll records and essentially "mine" the data for qualified employees and then file tax claims for refunds with the State.

In addition to the reforms listed above, there have been other reforms discussed that would limit the size of the enterprise zone program. However, the Governor's proposal to eliminate the enterprise zone program merits consideration given the state's fiscal situation and the lack of any evidence or performance data that the program provides any overall benefit to the state.

Staff Recommendation. Staff recommends that the Subcommittee hold this issue open.

Senate Budget and Fiscal Review— Mark Leno, Chair

SUBCOMMITTEE NO. 4 Agenda

Senator Michael J. Rubio, Chair
Senator Doug LaMalfa
Senator Noreen Evans

Agenda – Part A

Hearing Outcomes

Thursday, February 10, 2011
9:30 a.m. or upon adjournment of session
Room 112

Consultant: Brian Annis

Item Number and Title **Page**

Proposed Discussion / Vote Issues:

(See Table of Contents on page 1 for a more specific listing of issues)

AGENDA – DISCUSSION / VOTE ITEMS

Item **Department**

Issues Suggested for Discussion / Vote:

0520 Secretary for Business, Transportation and Housing

Department Overview: The Secretary of the Business, Transportation and Housing Agency (BT&H Agency) is a member of the Governor's Cabinet and oversees 16 departments, including the following large departments:

- Alcoholic Beverage Control
- Corporations
- Housing and Community Development
- California Highway Patrol
- Motor Vehicles
- Financial Institutions
- Real Estate
- Managed Health Care
- Transportation

In addition, the Secretary's Office oversees programs, including the following, which are budgeted directly in the Secretary's Office:

- Infrastructure and Economic Development Bank
- Film Commission
- Small Business Loan Guarantee Program
- Tourism Commission

Budget Overview: The Governor proposes total expenditures of $100.9 million ($4.2 million General Fund) and 60.7 positions for the Office of the Secretary – an increase of $78.2 million from the adjusted 2010-11 budget, and an increase of 1.5 funded positions. The primary reason for the year-over-year change is a one-time federal grant of $84.4 million to support the Small Business Loan Guarantee Program.

(See budget issue on next page)

Issue 1 – Small Business Loan Guarantee Program Expansion (BCP #2)

Governor's Budget Request. The Governor requests various budget changes related to a federal grant award that will result in one-time funding of $84.4 million for the Small Business Loan Guarantee Program (SBLG). This represents a significant expansion of the program which has typically had a trust-fund balance between $30 million and $40 million. The SBLG Program provides assistance to small businesses that may not qualify for traditional loans, by guaranteeing a portion of the loaned amount. The Administration requests to revert $20 million in General Fund support provided to the program one-time as part of the 2010 Budget Act (AB 1632, Chapter 731, Statutes of 2010). This reversion of $20 million is contingent on receipt of the federal funds. Finally, the Administration requests to double program staff from 1.5 positions to 3.0 positions.

Background / Detail. The Small Business Loan Guarantee Program is administered by 11 non-profit Financial Development Corporations (FDCs) via contracts with the State. In the current year, administration funding for the FDCs sum about $2.2 million ($1.7 million General Fund and $500,000 interest earnings) and the cost of the state oversight positions is about $150,000 (General Fund). The FDCs additionally charge fees in the range of 1 – 3 percent on the loan guarantees – which, with the federal money, could provide administration funding of the magnitude of $5 million depending on the volume of guarantees. The trust fund itself currently has a balance of about $44 million, and loan guarantees must not exceed five times the balance of the trust fund. In recent years, the SBLG Program has experienced significant fluctuation in General Fund support, trust fund earnings, and even a temporary suspension in new loan activities due to a prior reversion to the General Fund. The $84 million in federal funds would support the program at a new peak level, and would arrive in three parts over time – about $28 million should be received by the end of 2010-11.

Staff Comment: The federal funds allow the state to expand this program, which is popular in many communities, and at the same time realize a General Fund benefit of $20 million by reverting the augmentation provided last year. This baseline proposal appears to be a "win-win" for the program and State General Fund. The budget question that may merit consideration of the Subcommittee is what level of staffing is appropriate, and can additional General Fund relief be realized from substituting these new federal funds for base program funding and trust fund balances. Specifically:

- Can the state perform program oversight with fewer than 3.0 positions?
- Can the base $1.9 million General Fund support for state administration and the FDCs, be reduced or deleted and backfilled with federal funds?
- Can the base trust fund balance of $24 million be reverted to the General Fund immediately, or over time, and backfilled with federal funds?

LAO Recommendation: The Analyst recommends the Legislature:
a) Adopt the Governor's proposal to revert $20 million to the General Fund.

b) Adopt trailer bill language (TBL) to allow for the reversion of the additional General Fund dollars as the lines of credit and loans backed by roughly $24 million in state funds expire.
c) Reduce the request for additional staff by one and approve the 0.5 managerial position.
d) Consider eliminating the $1.7 million General Fund subsidy provided to FDCs.

Staff Recommendation:

a) Adopt the Governor's proposal (and LAO recommendation) to revert $20 million to the General Fund.
b) Reject LAO recommendation to adopt TBL to revert base trust fund assets (about $24 million) to the General Fund, but adopt TBL to direct that new loan guarantees use federal funds first.
c) Adopt the LAO recommendation to approve 0.5 new staff instead of 1.5 new staff.
d) Reject LAO recommendation to eliminate General Fund support for administration, and rather convert program administration funding to 50-percent General Fund and trust fund interest, and 50-percent federal funds, which is proportional to new program resources. (In the out-years, the administration funding share could be adjusted again to reflect program resources after the full federal grant is received. This staff recommendation would provide additional FDC administration funding over the base level for ramp-up, but still result in General Fund expenditure savings of about $1.0 million).

Action: On a 3 – 0 vote, adopted the staff recommendation, but additionally adopted budget bill language that would allow the Director of Finance to transfer up to $20 million from the GF to the Trust Fund if loan defaults reduce the trust fund balance to the extent additional funds are necessary to maintain a 5:1 reserve ratio for outstanding loans. Joint Legislative Budget Committee (JLBC) notification would be required.

8880 Financial Information System for California

Department Overview: The Financial Information System for California (FI$Cal), is an Enterprise Resource Planning (ERP) information technology (IT) project intended to replace, consolidate, and upgrade multiple legacy financial systems with a single system that would encompass the areas of: budgeting; accounting; procurement; cash management; and financial management. The development of FI$Cal resides with four “Partner Agencies”: the Department of Finance, the State Treasurer's Office, the State Controller's Office, and the Department of General Services. The FI$Cal system will be implemented in several phases, or “waves,” over the next decade. Budget Control Section 8.88 is a technical fiscal provision that directs special funds to the FI$Cal project and it will be made to conform to the final budget adopted under the 8880 budget items.

Budget Overview: The Governor proposes $70.8 million ($20.9 million General Fund) for continuing the FI$Cal project. This represents a year-over-year increase of $29.0 million ($5.2 million General Fund). Funded positions would grow from 62.1 to 95.9. The reason for the funding increase is that the project would be moving into the implementation stage with contract award to the vendor by December 31, 2011. The 12-year cost of fully implementing the project is estimated at $1.6 billion (both General Fund and other funds). The Administration is exploring financing options such as bonding and vender-financing to spread costs over a longer period.

(See budget issue on next page)

Issue 1 – FI$Cal Budget Request for 2011-12 (BCP #1)

Governor's Budget Request: As indicated above, the Governor requests $70.8 million ($20.9 million General Fund) for the project in 2011-12. The next 12 months are a critical time for the project, with key decision points on whether to move forward with the project as currently configured, how to finance the project, and to which vendor to award the integration contract. Current law (Government Code 15849.21) requires a report to the Legislature and 90-day review by the Joint Legislature Budget Committee (JLBC), after a contract is negotiated with the winning bidder, but prior to contract award – this report is anticipated in the July to September period of this year.

Project Timeline: Currently, three selected vendors are completing the "Fit-Gap," or stage I contract, which involves a review of potential gaps between the vendor's software and the state's business requirements. Project staff have also asked the three vendors to propose financing options and have held discussions with the State Infrastructure Bank (I-Bank) on financing options. The following are key upcoming dates:

- February 2011 – Financing proposals due from vendors.
- March 2011 – Fit-Gap or Stage I proposals due and begin negotiations.
- July 2011 – Select winning contractor and proceed on final negotiations.
- August 2011 – Deliver Special Project Report #4 and report to JLBC. The JLBC report is required to include costs and benefits of alternative approaches to the implementation of the FI$Cal system, including, but not limited to, a scaled-back version of the system.
- December 2011 (or earlier) – Award contract.
- January 2012 – Ramp up project and costs - $20 million for contractor, $12.7 for State Office of Technology Service, hire 33 new positions, and other activities included in the BCP.

Staff Comments: As the timeline above indicates, there will be new information and legislative reporting coming over the next few months and in the late summer / early fall. Some of this information will be available as the Subcommittee continues with budget hearings in April and May. Other information will only come after the budget is passed and the new fiscal year begins on July 1. Due to this schedule, the Subcommittee may wish to consider holding final action on the FI$Cal budget until later this spring. Because the report to the Legislature will not arrive until after the budget is passed, the Legislature will want to carefully consider budget bill language, or trailer bill language, to maintain appropriate legislative funding control after the proposed-contract detail is provided.

Staff Recommendation: Hold open for future consideration in the spring after further detail is available on alternative financing options.

Action: No action taken. Issue to be considered further in the spring.

California Alternative Energy and Advanced Transportation Financing Authority (0971)

Department Overview: The mission of the California Alternative Energy and Advanced Transportation Financing Authority (CAEATFA) is to promote the prompt and efficient development of energy sources which are renewable or which more efficiently utilize and conserve scarce energy resources.

Budget Overview: The January Governor's Budget proposed total funding of $25.8 million (special funds and reimbursements) and 7.0 positions, an increase of $9.2 million and no change in positions. The year-over-year increase is primarily explained by the implementation of California Ethanol Producers Incentive Program (See Issue 1 on the following page for detail on this budget request).

Informational Note on the PACE Program: Due to a continuous appropriation enacted last year, the CAEATFA budget includes a $15 million transfer from the Renewable Resource Trust Fund related to the Property Assessed Clean Energy Program (PACE). The PACE Program provides up-front financing for renewable and energy efficiency-related upgrades to properties with a unique financing mechanism of a loan that is backed by the property and transferable to new owners if the property changes hands. Recent state legislation, SB 77 (Chapter 15, Statutes of 2010, Pavley), facilitated program participation by small local governments by allowing them to pool PACE bonds via CAEATFA before going to market. The federal government has recently determined that the PACE program presents significant safety and soundness concerns that must be addressed by Fannie Mae, Freddie Mac, and the Federal Home Loan Banks. The federal action effectively halted the operation of PACE programs while the legal issues now proceed to the courts. The Legislative Analyst recommends that the Legislature reverse the $15 million transfer, without prejudice, pending legal resolution of the issue that has suspended PACE activity. Staff suggests no action at this time, as the PACE issue may be addressed in a policy bill, or may be better informed by review in Budget Subcommittee #2 which oversees energy-related budget issues. This Subcommittee can revisit this issue at a later date as warranted.

(See budget issue on next page)

Issue 1 – AB 118 / Ethanol Producers Incentive Program (BCP#1)

Governor's Request: The Administration requests $9 million in reimbursement authority for CAEATFA to receive funds from the California Energy Commission (CEC) to perform activities related to the Alternative and Renewable Fuel and Vehicle Technology Program as authorized by AB 118 (Chapter 750, Statutes of 2007, Nunez). The specific program is the California Ethanol Producer Incentive Program whereby financial assistance is provided to ethanol producers selected by CEC to develop and commercialize advanced transportation technologies that meet advanced energy goals.

Background/Detail: AB 118 authorizes the CEC to implement various programs consistent with the most recently adopted Investment Plan for the Alternative and Renewable Fuel and Vehicle Technology Program. Pursuant to the 2010 Budget Act, CAEATFA and the CEC are entering into an interagency agreement that outlines the terms by which CAEATFA will assist CEC in implementing the ethanol incentive program goals. The interagency agreement is expected to have a 4-year term expiring in January 2015. The terms of the agreement require CEC to transfer a total of $15 million.

Staff Comment: The Governor's budget reflects a $15 million reimbursement in 2010-11 and a $9 million reimbursement in in the budget year. The two-year amount requested exceeds the interagency agreement by about $9 million – CAEATFA indicates this is proposed due to uncertainty about how funds will be distributed across fiscal years and to maximize flexibility.

LAO Recommendation: The Legislative Analyst recommends holding action on this item pending receipt of the 2011-12 AB 118 Investment Plan, which should be submitted to the Legislature this March. The Legislature has expressed a great deal of interest in the AB 118 program administered by CEC, and as such, has statutorily required that the CEC annually submit an AB 118 Investment Plan. This requirement is designed to improve the Legislature's oversight of the AB 118 program.

Staff Recommendation: Deny without prejudice to defer final consideration of this request to later this spring after the AB 118 report has been provided and reviewed.

Action: Denied budget request without prejudice to defer final consideration to spring budget hearings.

9620 Cash Management and Budgetary Loans

Department Overview: This budget item appropriates funds to pay interest costs on General Fund borrowing used to overcome cash flow imbalances during the fiscal year. Because receipts and disbursements occur unevenly throughout the fiscal year, the General Fund borrows in most years, even though each budget is balanced when enacted and funds are repaid within the fiscal year. Interest is paid on both internal borrowing (such as cashflow loans from special funds) and for external borrowing (such as Revenue Anticipation Notes [RANs]). This item additionally pays interest costs for budgetary borrowing by the General Fund from special funds. Budgetary borrowing is across fiscal years and is scored as a budget solution, whereas cashflow borrowing is not counted as a budget solution (only a cash solution).

Budget Overview: The January Governor's Budget includes $300 million for interest costs on cashflow borrowing and $62 million for interest costs on budgetary borrowing – all General Fund. Of the cashflow amount, $100 million is for internal borrowing and $200 million is for external borrowing. Overall, expenditures in this item are up significantly – a total of $362 million is proposed for 2011-12, versus revised expenditures of $230 million in 2010-11. The year-over-year difference is primarily explained by the late budget last year that delayed the RAN sale until late in 2010. The Administration assumes the 2011-12 RAN sale will occur in July, resulting in a longer borrowing period and higher interest costs.

(see budget issues on next page)

Issue 1 – Intra-year Payment Deferrals / Cashflow Loans (Trailer Bill Language)

Governor's Proposal: The Administration requests statutory change that would allow intra-year cash payment deferrals in 2011-12, which would be similar to the authority granted for 2010-11. These deferrals represent an additional cashflow solution that have been necessary even after internal and external cashflow borrowing. The language also allows cashflow loans from two additional funds: the Immediate and Critical Needs Account in the State Court Facilities Construction Fund and the Hospital Quality Assurance Revenue Fund.

Background: Last year's cashflow measures were enacted by three bills: AB X8 5; AB X8 14; and AB 1624. The 2010-11 legislation provided approximately $5 billion in cashflow relief, and this year's proposal would be reduced to about $4.5 billion, due to the prohibition placed on borrowing from certain transportation funds by Proposition 22 of 2010. Last year's deferral plan was developed in consultation with higher education and local governments to minimize negative consequences. Finally, the plan includes triggers, such that the deferrals will not occur if the team of the State Treasurer, the State Controller, and the Director of Finance concur they are not necessary to maintain cash balances for the State. Cashflow loans are allowed for most special funds and existing statute requires repayment as needed for the program.

Detail: As indicated above, the Governor's proposal for 2011-12 is very similar to the enacted plan for 2010-11. The following are the major statutory components:

- K-12 Education – Permits up to 3 deferral periods not to exceed $2.5 billion at any one time. Includes a hardship-exemption process for certain local education agencies.
- Community College – Permits deferrals up to $200 million.
- California State University – permits deferrals up to $250 million.
- Cities and Counties – permits deferrals of specified payments to local governments not to exceed $1 billion.

Through existing administrative authority (no statutory change needed), the Administration could also defer $500 million to the University of California and about $81 million of CalWORKs administrative funding to counties.

Staff Comment: The Department of Finance should explain the need for the cash deferrals in 2011-12 and explain how the 2011-12 plan would compare and contrast to the 2010-11 plan. While cash deferrals to other government units are not desirable, they appear necessary for 2011-12 to avoid payment deferrals to private vendors and taxpayers (such as vendor payments and delayed tax refunds).

Staff Recommendation: Approve the placeholder trailer bill language.

Action: Approved the Administration's placeholder trailer bill language.

Issue 2 – Repayment of Special Fund Loans (Governor's Budget)

Governor's Proposal: As indicated in the introduction to this issue, the January Governor's Budget requests $62 million General Fund to pay interest on outstanding special-fund loans – this is budgeted in item 9620. Interest is only repaid when the loan principal is repaid. The amount of principal repaid is $566 million; however, principal repayment is budgeted as a revenue adjustment instead of an expenditure. The amount of total special fund loans outstanding as of December 31, 2010, is $2.6 billion, according to the Department of Finance. This table below reflects the Administration's planned special-fund loan repayments in 2011-12 (dollars in millions).

Fund Name	Principal	Interest
Accountancy Fund	$10,000,000	$84,521
Contractors' License Fund	10,000,000	727,003
State Dentistry Fund	3,000,000	739,688
Occupational Therapy Fund	640,000	79,627
Enhanced Fleet Modernization Subaccount	20,000,000	169,041
Public School Planning, Design, and Construction Review Revolving Fund	10,000,000	727,003
Housing Rehabilitation Loan Fund	9,200,000	965,526
Rental Housing Construction Fund	500,000	72,762
State Highway Account, State Transportation Fund	200,000,000	19,566,247
Bicycle Transportation Account, State Transportation Fund	6,000,000	586,987
Local Airport Loan Account	7,500,000	733,734
Motor Vehicle Fuel Account, Transportation Tax Fund	8,000,000	782,650
Environmental Enhancement and Mitigation Program Fund	4,400,000	430,457
Historic Property Maintenance Fund	3,000,000	293,494
Pedestrian Safety Account, State Transportation Fund	1,715,000	167,781
Motor Vehicle Account	40,000,000	338,082
Beverage Container Recycle Fund	88,000,000	21,697,524
Tire Recycling Management Fund	27,097,000	2,914,531
Recycling Market Development Revolving Loan Subaccount	1,853,000	248,918
Universal Lifeline Telephone Service Trust Administrative Committee Fund	45,000,000	3,271,512
Deaf and Disabled Telecommunications Program Administrative Committee Fund	30,000,000	2,181,008
Teleconnect Fund	40,000,000	5,373,288
	$565,905,000	**$62,151,384**

Staff Comment: The Department of Finance should present their special-fund loan repayment plan and the LAO should comment. Generally, decisions about special fund loans will be made in the budget Subcommittees by subject-matter area, although the 9620 Budget Item should be made to conform.

Governor's February 9, 2011, Budget Revision: On February 9, 2011, Governor Brown canceled the sale-leaseback of 11 state office buildings and proposed to backfill for the General Fund loss with new special fund loans, repayment deferrals, and other measures. The new solutions total $1.2 billion. Full detail on that proposal was not available at the time this agenda was finalized, but staff has asked the Department of Finance to present a summary of the revised plan at the hearing.

Staff Recommendations: Take no action, this is an informational issue.

Action: Informational – no action taken.

9100 Tax Relief

Action: On a 3 – 0 vote, rejected the Governor's proposal for Williamson Act open-space subventions, and funded at the $20 million level in 2011-12. (Funding of $10 million restored for 2010-11.)

Senate Budget and Fiscal Review— Mark Leno, Chair

SUBCOMMITTEE NO. 4 Agenda

Senator Michael J. Rubio, Chair
Senator Doug LaMalfa
Senator Noreen Evans

Thursday, February 3, 2011
9:30 a.m. or upon adjournment of session
Room 112

Consultant: Brian Annis

(See Table of Contents on page 1 for a more specific listing of issues)

Pursuant to the Americans with Disabilities Act, individuals who, because of a disability, need special assistance to attend or participate in a Senate Committee hearing, or in connection with other Senate services, may request assistance at the Senate Rules Committee, 1020 N Street, Suite 255 or by calling 916-324-9335. Requests should be made one week in advance whenever possible.

AGENDA – VOTE ONLY ITEMS

AGENDA – DISCUSSION / VOTE ITEMS

Issues Suggested for Vote Only:

California Tax Credit Allocation Committee (0968)

Department Overview: The mission of the California Tax Credit Allocation Committee (CTCAC) is to fairly allocate federal and state tax credits to create and maintain safe quality affordable rental housing for low-income households in California by forming partnerships with developers, investors, and public entities.

Budget Overview: The Governor's Budget proposes total funding of $5.2 million (no General Fund) and 37.0 positions, an increase of $412,000 and an increase of 2 positions.

Issue 1 – Staff Positions for federal requirements (BCP#1)

Governor's Budget Request: The Administration requests $282,000 (special funds) and the establishment of two new Associate Governmental Program Analyst positions and contract funding for federal reporting related to the Housing and Economic Recovery Act of 2008 and the American Recovery and Reinvestment Act (ARRA) of 2009.

Detail: The CTCAC indicates that the workload relates to new reporting requirements instituted by the federal government on June 23, 2010. Specifically, CTCAC must now obtain "tenant specific data" such as race, ethnicity, age, disability status, income, family composition, use of rental assistance under Section 8, and monthly rental payments for each household member in each tax credit unit in each tax credit project in CTCAC's portfolio of over 3,055 tax credit properties which include 266,417 rental units. Additionally, ARRA requires additional asset monitoring activity. CTCAC cites risk of non-compliance and loss of federal funds if the required reporting is not performed.

Staff Recommendation: Approve the budget request.

Vote:

Issues Suggested for Discussion / Vote:

9210 Local Government Financing

Department Overview: The 9210 budget item includes several programs that include State subventions to local governments for such purposes as health, welfare, and public-safety programs. The public safety funding issues are heard in Subcommittee #5 and constitute most of the budget funding in this item. The topics heard in Subcommittee #4 include interest payments on 2009-10 "Prop 1A" borrowing from local governments – about $90.8 million; and a small subvention to Redevelopment Agencies (RDAs) to help retire a portion of outstanding debt that was backed by the personal property tax – about $500,000. Budget issues related to local government finance, such as shifts or borrowing of local property tax, are also heard under this item.

Budget Overview: The proposed budget for the 9210 item is $551 million General Fund, which is similar to the adjusted 2010-11 level. About $455 million of this amount is related to public safety and heard in Subcommittee #5. The remaining $90 million is heard in Subcommittee #4. Prop 1A interest and RDA personal property tax subventions are ongoing, non-controversial, issues. However, the Governor has proposed a significant budget change this year via the elimination of RDA's –that issue is presented for discussion on the following page.

(See budget issue on next page)

Issue 1 – Elimination of Redevelopment Agencies (Governor's Budget)

Governor's Request: The Governor proposes to eliminate redevelopment agencies (RDAs). This elimination would provide a State General Fund solution of $1.7 billion in 2011-12 by shifting a portion of RDA tax increment to offset General Fund costs for trial courts and Medi-Cal. In 2012-13 and thereafter, the non-obligated portion of RDA tax increment – that revenue not needed for outstanding debt and contractual obligations – would flow instead to K-14 schools, cities, counties, and non-enterprise special districts. To facilitate replacement revenue for local economic development, the Governor proposes to lower the vote threshold to 55 percent for specified local tax increases if the revenue is directed to infrastructure.

Background on Redevelopment: Existing law authorizes cities and counties to create a redevelopment project area to address urban blight. Redevelop and "tax-increment financing," which is bonding against future growth in property tax revenue in an RDA area, have existed in California since the 1950s. RDAs are required to set aside 20 percent of their income to help build affordable housing. The RDA share of property tax revenue has grown substantially from 4 percent in 1983-84 to 12 percent currently and the current level of annual increment revenue is about $5 billion. As the RDA share of property tax has increased, the proportion available for schools and other local governments has decreased. The amount lost to the schools is about $2 billion, and because the State backfills the school revenue, this is an annual General Fund cost of about $2 billion.

Detail on the Governor's Proposal: As indicated, the Governor's proposal would eliminate RDAs. However, because RDA's have outstanding debt service and other contractual obligations, the Governor proposes to create successor entities to administer these obligations. The increment revenue necessary for these outstanding obligations would be directed to these successor entities. The Administration estimates these remain obligations, and existing "pass-through" payments to other local governments would total about $3.3 billion in 2011-12. The remaining $1.9 billion of increment revenue would be allocated $1.7 billion to offset State General Fund costs for trial courts and Medi-Cal, and $210 million to cities and counties. In 2012-13 and thereafter, all the non-obligated increment funds would be directed to schools and local governments, with none directed to State General Fund relief. The K-14 funding would be separate from the Proposition 98 funding calculation, and would be net new revenue for schools. Cities, counties, and non-enterprise special districts would receive new revenue to support their public safety and other functions. The Governor proposes that any existing balances reserved for low and moderate income housing be shifted to local housing authorities for those same purposes.

Proposition 22 and Constitutional Issues: In 2009-10 and 2010-11, a total of $2 billion was shifted from RDA's to local schools using a mechanism that provided the State General Fund with expenditure offsets of the same amount. The California Redevelopment Association was opposed to the 2009-10 and 2010-11 shifts, and was a supporter of Proposition 22, which was approved by voters on the November 2, 2010, ballot. Proposition 22 prohibits the Legislature from enacting statute that would redirect RDA funds to benefit the State. The Governor's plan would eliminate RDAs, and in doing so, the Administration believes the proposal is not in conflict with Proposition 22 or other constitutional provisions.

What the Opponents of the Proposal Say: The California Redevelopment Association in a January 10, 2011, press release indicates redevelopment is a vital local government tool in revitalizing blighted communities and bringing them back to economic vitality by creating jobs, funding affordable housing, building public infrastructure improvements, and creating commercial opportunities. Further, if redevelopment were eliminated, it will have a direct and lasting negative impact on the California economy.

What the Administration Says: The Governor's Budget Summary indicates that the private development that occurs in redevelopment project areas often would have occurred even if the RDAs were never established. While (RDAs) may help relieve localized blight and equalize economic activity related to nearby communities, there are better alternatives for local entities to fund these efforts without shifting resources from schools, counties, special districts, and core city services.

Staff Comment: The Legislative Analyst has prepared a summary of the Governor's proposal. The LAO can present this summary at the hearing and highlight what they think are the key issues for consideration. The Department of Finance will also be available at the hearing to explain the legal and implementation details of the proposal.

Staff Recommendation: Hold open for action in the Full Budget Committee. This issue is a major component of the Governor's budget solution, and should be considered in the full context of the Governor's other expenditure and revenue solutions, and any alternative budget solutions that the Full Budget Committee may wish to consider. Additionally, the Senate Governance and Finance Committee will hear this issue on February 9, and that hearing should result in additional analysis and discussion to further inform the decision on this proposal.

9100 Tax Relief

Department Overview: The 9100 budget item includes several programs that provide property tax relief by making payments to local governments to help defray revenues lost as a result of tax relief programs. There are currently two tax relief programs in this item, and the funding amount indicated is the amount of General Fund proposed for 2011-12:

- Homeowners' Property Tax Relief ($442.2 million)
- Subventions for Open Space / Williamson Act ($1,000)

The Homeowners' Property Tax Relief program is constitutionally required, and therefore is fully funded. The Williamson Act program is a discretionary program and funding has either been eliminated or reduced in recent budget years.

Budget Overview: The estimated funding level for Homeowners' Property Tax Relief is unchanged from the adjusted 2010-11 level of $442.2 million. Williamson Act funding is proposed at $1,000 to suspend state payments. It is budgeted at $1,000 instead of $0 due to a technical budget issue and the need to suspend a continuous appropriation that exists in current statute. Governor Schwarzenegger vetoed program funding to $1,000 in the 2009 Budget Act. A trailer bill to the 2010 Budget Act (SB 863) appropriated $10 million for the program, but the proposed budget would also eliminate this 2010-11 funding. Full funding for the Williamson Act would cost about $40 million.

Issue 1 – Williamson Act Open-Space Funding (Trailer Bill Language)

Governor's Request: The Governor proposes to eliminate the Williamson Act Open-Space subvention payment for both 2010-11 and 2011-12 and scores a General Fund (GF) budget savings of $10 million in each year.

Background: The Williamson Act allows cities and counties to enter into contracts with landowners to restrict certain property to only open space and agricultural uses. The land is restricted in use for 10 or 20 years depending on the type of contract. In return for these restrictions, the property owners pay reduced property taxes because the land is assessed at a lower-than-market level. The State then *partially* compensates the local governments for their related property tax loss. In addition to the direct cost of Williamson Act subventions, the State incurs additional costs from backfilling K-14 schools for their reduced property tax receipts under the Proposition 98 minimum guarantee for K-14 education funding. The following table shows recent funding for Williamson Act by fiscal year (dollars in millions)

Fiscal Year	Prop 98 GF Cost*	Williamson Subvention	Total State GF Cost	Comment
2007-08	$40.0	$37.6	$77.6	Fully Funded
2008-09	$40.0	$33.8	$73.8	10% Cut
2009-10	$40.0	$0	$40.0	Suspended
2010-11 (as enacted)	$40.0	$10	$50.0	Modified Funding Program
2010-11 (proposed)	$40.0	*$0*	*$40.0*	*Suspended*
2011-12 (proposed)	$40.0	*$0*	*$40.0*	*Suspended*

* LAO estimate, actual unknown. Prop 98 education backfill continues in the short run even when the Williamson subvention is suspended. Over the longer run, the Prop 98 backfill cost would fall if counties do not renew contracts.

LAO Comment: The LAO has questioned the cost-effectiveness of the subvention program in prior analyses. The LAO indicates the Governor's proposal warrants approval.

Staff Comment: Suspension of funding does not prohibit land owners and counties from continuing to renew Williamson Act contracts. However, some counties have indicated they will not renew contracts if the state does not provide the subvention.

Staff Recommendation: Hold open for consideration in the full Budget Committee.

Commission on State Mandates (8885)

Department Overview: The Commission on State Mandates (Commission) is responsible for determining whether a new statute, executive order, or regulation contains a reimbursable state mandate on local governments and determining the appropriate reimbursement to local governments from a mandate claim. This budget item appropriates the funding for the staff and operations costs of the Commission, and appropriates non-education mandate payments to local governments. The Constitution, as amended by Proposition 1A of 2004, requires that the Legislature either fund or suspend local mandates – in most cases, if the Legislature fails to fund a mandate, the legal requirements are considered suspended pursuant to the Constitution. Payments for mandate costs incurred prior to 2004 are one exception noted in the Constitution, as are mandates related to labor relations.

Budget Overview: The January Governor's Budget proposed expenditures of $56.7 million ($53.7 million General Fund) and 11.0 positions, a decrease of about $27.9 million over the adjusted current-year budget and no change in positions. It should be noted, the 2010-11 adjusted funding level is after the prior Governor's veto of $131 million. The Governor's budget includes the continuation of certain mandate suspensions, some new mandate suspensions, and deferrals of mandate payments to generate General Fund savings of about $321.7 million. The savings measures include: (1) savings of $94.0 million by deferring payment of pre-2004 mandate claims; (2) savings of $172.6 million by suspending certain local mandates; and (3) savings of $55.1 million from deferring payment on expired mandates or some mandates exempt from the requirements of Proposition 1A of 2004. Under (2) above, most mandates are proposed for suspension except those related to law enforcement and tax collection.

Proposed Mandate Funding in Governor's Budget—General Fund

Title	Amount (000s)
Allocation of Property Tax Revenue	596
Crime Victim's Domestic Violence Incident Reports	188
Custody of Minors-Child Abduction and Recovery	13,999
Domestic Violence Arrests and Victim's Assistance	2,565
Domestic Violence Arrest Policies	7,412
Domestic Violence Treatment Services	2,345
Health Benefits for Survivors of Public Safety Officers	1,526
In-Home Support Services II	491
Medical Beneficiary Death Notices	27
Peace Officer Personnel Records	543
Rape Victim Counseling	376
Sexually Violent Predators	21,908
Threats Against Police Officers	40
Unitary Countywide Tax Rates	244
Total	$52,259

Informational Note: Most of the budget proposals in this area are continuations of budget actions taken over the past few years, such as the deferral in payment of pre-2004 mandate claims. Most mandates have been suspended for multiple years to reduce General Fund costs. The mandates that are presented in this agenda are those that are new proposals or involve new issues. The Governor has proposed to fund one mandate – mental health services for students, or the AB 3632 mandate – within the realignment proposal using Proposition 63 funds. The AB 3632 proposal is being considered by Subcommittee #1.

(See budget issue on next page)

Issue 1 – Elections-Related Mandates

Governor's Request: The Governor proposes suspension of the elections-related mandates for the 2011-12 fiscal year. The Administration estimates this action would result in General Fund savings of about $31 million, although this amount may change after February claims are received. Most of the costs associated with these mandates involve postage and administration costs for absentee ballots, although certain voter-registration procedures are also mandates.

Staff Comment: These elections-related mandates have not been suspended in prior years because there has been concern about how suspension would affect the uniformity of statewide elections. If the mandates are suspended and if individual counties choose to modify their elections procedures, voters could see differential treatment depending on their county of residence.

Staff Recommendation: Keep issue open.

Issue 2 –Brown Act / Open Meeting Mandates

Governor's Request: The Governor proposes suspension of the Brown Act mandates for the 2011-12 fiscal year. The Administration estimates this action would result in General Fund savings of about $63 million, although this amount may change after February claims are received. These mandates require local government to post agendas three-days prior to public hearings and to disclose actions taken in closed sessions. One might think this mandate would be inexpensive – with costs such as the cost of paper, but the state is billed for the time local employees spend drafting such agendas, legal review of the documents, etc.

State Constitution Requires Open Government: Proposition 59 of 2004, amended Article I, Section 3 of the California Constitution to state that the people have the right of access to information concerning the conduct of the people's business, and therefore, the meetings of public bodies and the writings of public officials and agencies shall be open to public scrutiny. Voter-approved mandates do not require state reimbursement, but due to difference in specificity between statute and the Constitution, the reimbursement is currently considered required.

Options to Protect Open Meetings, but Save State Costs: Last year, the Budget Conference Committee adopted trailer bill language that would repeal and reenact relevant provisions of the Brown Act to be best practices for compliance with Proposition 59. This action was thought to be a mechanism to relieve the state's reimbursement requirement but still maintain the current open government practices. That provision was stripped from final trailer bill language as the measure moved to a final vote, because opposition came forward with the fear that the statutory revisions would not be sufficient to maintain open-meeting practices. Another option to relieve state costs in the future would be to amend the Constitution to add specificity. For example, Senate Constitution Amendment (SCA) 7 (Yee), would add this sentence to the Constitution: *Each public body shall provide public notice of its meetings and shall publicly disclose any action taken*.

Current Status of the Brown Act: The Department of Finance has stated that the Brown Act is suspended for 2010-11. While the 2010 budget bill did not list the Brown Act as suspended, it also did not list the Brown Act as funded – this was consistent with the original "best-practices" trailer bill approach. Staff is not aware of any local agencies that have changed their open meeting practices due to the current status of the mandate.

Staff Comment: It is clear from budget hearings over the past few years that the Legislature does not want to diminish open meeting requirements. Efforts have focused on retaining these practices while relieving the state cost of reimbursement. Due to ongoing General Fund pressures and a $63 million cost in 2011-12, a Constitutional amendment may be a good solution for consideration.

Staff Recommendation: Keep issue open.

0520 Secretary for Business, Transportation and Housing

Department Overview: The Secretary of the Business, Transportation and Housing Agency (BT&H Agency) is a member of the Governor's Cabinet and oversees 16 departments, including the following large departments:

- Alcoholic Beverage Control
- Corporations
- Housing and Community Development
- California Highway Patrol
- Motor Vehicles
- Financial Institutions
- Real Estate
- Managed Health Care
- Transportation

In addition, the Secretary's Office oversees programs, including the following, which are budgeted directly in the Secretary's Office:

- Infrastructure and Economic Development Bank
- Film Commission
- Small Business Loan Guarantee Program
- Tourism Commission

Budget Overview: The Governor proposes total expenditures of $100.9 million ($4.2 million General Fund) and 60.7 positions for the Office of the Secretary – an increase of $78.2 million from the adjusted 2010-11 budget, and an increase of 1.5 funded positions. The primary reason for the year-over-year change is a one-time federal grant of $84.4 million to support the Small Business Loan Guarantee Program.

(See budget issue on next page)

Issue 1 – Small Business Loan Guarantee Program Expansion (BCP #2)

Governor's Budget Request. The Governor requests various budget changes related to a federal grant award that will result in one-time funding of $84.4 million for the Small Business Loan Guarantee Program (SBLG). This represents a significant expansion of the program which has typically had a trust-fund balance between $30 million and $40 million. The SBLG Program provides assistance to small businesses that may not qualify for traditional loans, by guaranteeing a portion of the loaned amount. The Administration requests to revert $20 million in General Fund support provided to the program one-time as part of the 2010 Budget Act (AB 1632, Chapter 731, Statutes of 2010). Finally, the Administration requests to double program staff from 1.5 positions to 3.0 positions.

Background / Detail. The Small Business Loan Guarantee Program is administered by 11 non-profit Financial Development Corporations (FDCs) via contracts with the State. In the current year, administration funding for the FDCs sum about $2.2 million ($1.7 million General Fund and $500,000 interest earnings) and the cost of the state oversight positions is about $150,000 (General Fund). The FDCs additionally charge fees in the range of 1 – 3 percent on the loan guarantees – which, with the federal money, could provide administration funding of the magnitude of $5 million depending on the volume of guarantees. The trust fund itself currently has a balance of about $44 million, and loan guarantees must not exceed five times the balance of the trust fund. In recent years, the SBLG Program has experienced significant fluctuation in General Fund support, trust fund earnings, and even a temporary suspension in new loan activities due to a prior reversion to the General Fund. However, the $84 million in federal funds would support the program at a new peak level.

Staff Comment: The federal funds allow the state to expand this program, which is popular in many communities, and at the same time realize a General Fund benefit of $20 million by reverting the augmentation provided last year. This baseline proposal appears to be a "win-win" for the program and State General Fund. The budget question that may merit consideration of the Subcommittee is what level of staffing is appropriate, and can additional General Fund relief be realized from substituting these new federal funds for base program funding and trust fund balances. Specifically:

- Can the state perform program oversight with fewer than 3.0 positions?
- Can the base $1.9 million General Fund support for state administration and the FDCs, be reduced or deleted and backfilled with federal funds?
- Can the base trust fund balance of $24 million be reverted to the General Fund immediately, or over time, and backfilled with federal funds?

LAO Recommendation: The Analyst recommends the Legislature:

a) Adopt the Governor's proposal to revert $20 million to the General Fund.

b) Adopt trailer bill language to allow for the reversion of the additional General Fund dollars as the lines of credit and loans backed by roughly $24 million in state funds expire.
c) Reduce the request for additional staff by one and approve the 0.5 managerial position.
d) Consider eliminating the $1.7 million General Fund subsidy provided to FDCs.

Staff Recommendation:

a) Adopt the Governor's proposal (and LAO recommendation) to revert $20 million to the General Fund.
b) Reject LAO recommendation to adopt TBL to revert base trust fund assets to the General Fund, but adopt TBL to direct that new loan guarantees and renewed loan guarantees use federal funds first – as constrained by any federal rules.
c) Adopt the LAO recommendation to approve 0.5 new staff instead of 1.5 new staff.
d) Reject LAO recommendation to elimination General Fund support for administration, and rather convert program administration funding to 20-percent General Fund and trust fund interest, and 80-percent federal funds, which is proportional to new program resources (trust fund balances should be sufficient to result in no General Fund cost for 2011-12, for a General Fund expenditure savings of about $1.9 million).

Vote:

8880 Financial Information System for California

Department Overview: The Financial Information System for California (FI$Cal), is an Enterprise Resource Planning (ERP) information technology (IT) project intended to replace, consolidate, and upgrade multiple legacy financial systems with a single system that would encompass the areas of: budgeting; accounting; procurement; cash management; and financial management. The development of FI$Cal resides with four “Partner Agencies,” the Department of Finance, the State Treasurer's Office, the State Controller's Office, and the Department of General Services. The FI$Cal system will be implemented in several phases, or “waves,” over the next decade. Budget Control Section 8.88 is a technical fiscal provision that directs special funds to the FI$Cal project and it will be made to conform to the final budget adopted under the 8880 budget items.

Budget Overview: The Governor proposes $70.8 million ($20.9 million General Fund) for continuing the FI$Cal project. This represents a year-over-year increase of $29.0 million ($5.2 million General Fund). Funded positions would grow from 62.1 to 95.9. The reason for the funding increase is that the project would be moving into the implementation stage with contract award to the vendor by December 31, 2011. The 12-year cost of fully implementing the project is estimated at $1.6 billion (both General Fund and other funds). The Administration is exploring financing options such as bonding and vender-financing to spread costs over a longer period.

(See budget issue on next page)

Issue 1 – FI$Cal Budget Request for 2011-12 (BCP #1)

Governor's Budget Request: As indicated above, the Governor requests $70.8 million ($20.9 million General Fund) for the project in 2011-12. The next 12 months are a critical time for the project, with key decision points on whether to move forward with the project as currently configured, how to finance the project, and to which vendor to award the integration contract. Current law (Government Code 15849.21) requires a report to the Legislature and 90-day review by the Joint Legislature Budget Committee (JLBC), after a contract is negotiated with the winning bidder, but prior to contract award – this report is anticipated in the July – September period of this year.

Project Timeline: Currently, three selected vendors are completing the "Fit-Gap," or stage I contract, which involves a review of potential gaps between the vendor's software and the state's business requirements. Project staff have also ask the three vendor's to propose financing options and held discussion with the State Infrastructure Bank (I-Bank) on financing options. The following are key upcoming dates:

- February 2011 – Financing proposals due from vendors.
- March 2011 – Fit-Gap or Stage I proposals due and begin negotiations.
- July 2011 – Select winning contractor and proceed on final negotiations.
- August 2011 – Deliver Special Project Report #4 and report to JLBC. The JLBC report is required to include costs and benefits of alternative approaches to the implementation of the FI$Cal system, including, but not limited to, a scaled-back version of the system.
- December 2011 (or earlier) – Award contract.
- January 2012 – Ramp up project and costs - $20 million for contractor, $12.7 for State Office of Technology Service, hire 33 new positions, and other activities included in the BCP.

Staff Comments: As the timeline above indicates, there will be new information and legislative reporting coming over the next few months and in the late summer / early fall. Some of this information will be available as the Subcommittee continues with budget hearings in April and May. Other information will only come after the budget is passed and the new fiscal year begins July 1. Due to this schedule, the Subcommittee may wish to consider holding final action on the FI$Cal budget until later this spring. Because the report to the Legislature will not arrive until after the budget is passed, the Legislature will want to carefully consider budget bill language, or trailer bill language, to maintain appropriate legislative funding control after the proposed-contract detail is provided.

Staff Recommendation: Hold open for future consideration in the spring after further detail is available on alternative financing options.

California Alternative Energy and Advanced Transportation Financing Authority (0971)

Department Overview: The mission of the California Alternative Energy and Advanced Transportation Financing Authority (CAEATFA) is to promote the prompt and efficient development of energy sources which are renewable or which more efficiently utilize and conserve scarce energy resources.

Budget Overview: The January Governor's Budget proposed total funding of $25.8 million (special funds and reimbursements) and 7.0 positions, an increase of $9.2 million and no change in positions. The year-over-year increase is primarily explained by the implementation of California Ethanol Producers Incentive Program (See Issue 1 on the following page for detail on this budget request).

Informational Note on the PACE Program: Due to a continuous appropriation enacted last year, the CAEATFA budget includes a $15 million transfer from the Renewable Resource Trust Fund related to the Property Assessed Clean Energy Program (PACE). The PACE Program provides up-front financing for renewable and energy efficiency-related upgrades to properties with a unique financing mechanism of a loan that is backed by the property and transferable to new owners if the property changes hands. Recent state legislation, SB 77 (Chapter 15, Statutes of 2010, Pavley), facilitated program participation by small local governments by allowing them to pool PACE bonds via CAEATFA before going to market. The federal government has recently determined that the PACE program presents significant safety and soundness concerns that must be addressed by Fannie Mae, Freddie Mac, and the Federal Home Loan Banks. The federal action effectively halted the operation of PACE programs while the legal issues now proceed to the courts. The Legislative Analyst recommends the Legislature reverse the $15 million transfer, without prejudice, pending legal resolution of the issue that has suspended PACE activity. Staff suggests no action at this time, as the PACE issue may be addressed in a policy bill, or may be better informed by review in Budget Subcommittee #2 which oversees energy-related budget issues. This Subcommittee can revisit this issue at a later date as warranted.

(See budget issue on next page)

Issue 1 – AB 118 / Ethanol Producers Incentive Program (BCP#1)

Governor's Request: The Administration requests $9 million in reimbursement authority for CAEATFA to receive funds from the California Energy Commission (CEC) to perform activities related to the Alternative and Renewable Fuel and Vehicle Technology Program as authorized by AB 118 (Chapter 750, Statutes of 2007, Nunez). The specific program is the California Ethanol Producer Incentive Program whereby financial assistance is provided to ethanol producers selected by CEC to develop and commercialize advanced transportation technologies that meet advanced energy goals.

Background/Detail: AB 118 authorizes the CEC to implement various programs consistent with the most recently adopted Investment Plan for the Alternative and Renewable Fuel and Vehicle Technology Program. Pursuant to the 2010 Budget Act, CAEATFA and the CEC are entering into an interagency agreement that outlines the terms by which CAEATFA will assist CEC in implementing the ethanol incentive program goals. The interagency agreement is expected to have a 4-year term expiring in January 2015. The terms of the agreement require CEC to transfer a total of $15 million, starting with an initial transfer of $6 million in the current year and $9 million to be transferred once the initial amount is allocated by CAEATFA.

Staff Comment: The Governor's budget requests a $15 million increase in reimbursement and expenditure authority in the current year, and an increase of $9 million in the budget year. The two-year amount requested exceeds the interagency agreement by about $9 million – CAEATFA indicates this is proposed due to uncertainty about how funds will be distributed across fiscal years and to maximize flexibility.

LAO Recommendation: The Legislative Analyst recommends holding action on this item pending receipt of the 2011-12 AB 118 Investment Plan, which should be submitted to the Legislature this March. The Legislature has expressed a great deal of interest in the AB 118 program administered by CEC, and as such, has statutorily required that the CEC annually submit an AB 118 Investment Plan. This requirement is designed to improve the Legislature's oversight of the AB 118 program.

Staff Recommendation: Deny without prejudice to defer final consideration of this request to later this spring after the AB 118 report has been provided and reviewed.

Vote:

Debt Service General Obligation Bonds and Commercial Paper (9600)

Department Overview: Debt service payments are continuously appropriated, and therefore not appropriated in the annual budget bill. This item in the Governor's Budget displays the estimated debt service costs for each General Obligation bond (GO bond). Some bond costs are offset by special funds or federal funds – primarily by the transportation debt service fund. Other bonds are "self liquidating," or have their own dedicated revenue (i.e., the Economic Recovery Bonds [ERBs] receive a quarter-cent of the sales tax) – the self-liquidating bonds are not included in this item.

Budget Overview: The January Governor's Budget includes $4.9 billion in General Fund costs for GO debt service and related costs. In addition to this amount, $792 million in debt costs are funded from other funds (i.e., $778 million is from the transportation debt fund that is associated with the truck-weight-fee proposal). Finally, federal bond subsidies, through the Build America Bonds (BABs) program, provide $351 million in 2011-12. The table below, with data from the Governor's Budget, shows the three-year GO bond costs (in millions):

	2009-10 Actual Cost	**2010-11 Estimated Cost**	**2011-12 Estimated Cost**
General Fund cost	$4,639	$4,890	$4,927
Other funds cost	$239	$644	$792
Federal subsidy (Build America Bond Program)	$155	$300	$351
TOTAL Item 9600	**$5,033**	**$5,834**	**$6,070**
Economic Recovery Bonds (not included above)	$1,566	$1,351	$1,407

According to the Governor's Budget, the State has $79.8 billion in outstanding GO bond debt (including self-liquidating bonds). Another $39.6 billion in bonds is authorized, but unissued. The Governor's proposed budget includes $84.6 billion in General Fund expenditure, so GO bond debt service as a percentage of General Fund expenditures is 5.8 percent (or 7.5 percent when ERBs are included).

(see budget issue on next page)

Issue #1 - Deferral of Spring 2011 Bond Sale (Governor's Proposal)

Governor's Proposal: The Administration proposes to defer the spring 2011 bond sale until the fall, which would result in General Fund debt-service savings of approximately $248 million in 2011-12. During budget hearings last spring, the Schwarzenegger Administration had assumed a spring 2011 bond sale of $6.7 billion, but that number had been revised down to $3.5 billion in the Administration's fall estimate. This is not scored as a General Fund solution in the budget, because the assumption was built into the workload budget. The Administration now assumes $5.8 billion in bond sales this fall.

Detail: There has been some uncertainty among the various bond stakeholders about what the sales deferral means for individual bond programs. The Governor's budget explicitly cites a policy change to decrease Proposition 1C Housing bonds by $99 million in 2011-12 to reflect a one-time pause in new loans and grants for housing projects. Aside from the Proposition 1C statement, the Administration has told Committee staff that the remainder of bond programs should proceed as previously expected with cash balances from prior bond sales. Specifically, a cash balance of $13.3 billion from prior bond sales was on hand in December 2010, and that amount is expected to fund all underway bond projects through December 2011, and fund new project allocation that are planned to occur through June 2011 (including cash for those new projects also through December 2011). For projects expecting an allocation after June 2011, and for ongoing project cash needs after December 2011, the state would need to sell additional bonds this fall. The below table shows cash on hand by bond for some of the major bond acts (dollars in millions).

Bond Program	Cash, or bond proceeds, as of Dec 2010
Prop 1B of 2006: Transportation	$3,112
Prop 1E of 2006: Disaster Prep and Flood Prevention	$1,709
Prop 84 of 2006: Safe Drinking Water	$1,565
Prop 46 of 2002 &Prop 1C of 2006: Housing	$1,339
Prop 47 of 2002 & Prop 55 of 2004: Education Facilities	$1,249
Prop 71 of 2004: Stem Cell Research	$361
Prop 3 of 2008: Children's Hospital Bond Act	$341
Prop 1A of 2008: High Speed Rail	$245
All others	$3,406
TOTAL	**$13,327**

Staff Comment: The Administration should outline their plan for bond sales and how it will affect infrastructure projects under construction, and near construction.

Staff Recommendation: Take no action, this is an informational issue.

9620 Cash Management and Budgetary Loans

Department Overview: This budget item appropriates funds to pay interest costs on General Fund borrowing used to overcome cash flow imbalances during the fiscal year. Because receipts and disbursements occur unevenly throughout the fiscal year, the General Fund borrows in most years, even though each budget is balanced when enacted and funds are repaid within the fiscal year. Interest is paid on both internal borrowing (such as cashflow loans from special funds) and for external borrowing (such as Revenue Anticipation Notes [RANs]). This item additionally pays interest costs for budgetary borrowing by the General Fund from special funds. Budgetary borrowing is across fiscal years and is scored as a budget solution, whereas cashflow borrowing is not counted as a budget solution (only a cash solution).

Budget Overview: The January Governor's Budget includes $300 million for interest costs on cashflow borrowing and $62 million for interest costs on budgetary borrowing – all General Fund. Of the cashflow amount, $100 million is for internal borrowing and $200 million is for external borrowing. Overall, expenditures in this item are up significantly – a total of $362 million is proposed for 2011-12, versus revised expenditures of $230 million in 2010-11. The year-over-year difference is primarily explained by the late budget last year that delayed the RAN sale until late in 2010. The Administration assumes the 2011-12 RAN sale will occur in July, resulting in a longer borrowing period and higher interest costs.

(see budget issues on next page)

Issue 1 – Intra-year Payment Deferrals / Cashflow Loans (Trailer Bill Language)

Governor's Proposal: The Administration requests statutory change that would allow intra-year cash payment deferrals in 2011-12, which would be similar to the authority granted for 2010-11. These deferrals represent an additional cashflow solution that have been necessary even after internal and external cashflow borrowing. The language also allows cashflow loans from two additional funds: the Immediate and Critical Needs Account in the State Court Facilities Construction Fund, and the Hospital Quality Assurance Revenue Fund.

Background: Last year's cashflow measure were enacted by three bills: AB X8 5; AB X8 14; and AB 1624. The 2010-11 legislation provided approximately $5 billion in cashflow relief, and this year's proposal would be reduced to about $4.5 billion, due to the prohibition placed on borrowing from certain transportation funds by Proposition 22 of 2010. Last year's deferral plan was developed in consultation with higher education and local governments to minimize negative consequences. Finally, the plan includes triggers, such that the deferrals will not occur if the team of the State Treasurer, the State Controller, and the Director of Finance concur they are not necessary to maintain cash balances for the State. Cashflow loans are allowed for most special funds and existing statute requires repayment as needed for the program.

Detail: As indicated above, the Governor's proposal for 2011-12 is very similar to the enacted plan for 2010-11. The following are the major statutory components:

- K-12 Education – Permits up to 3 deferral periods not to exceed $2.5 billion at any one time. Includes a hardship-exemption process for certain local education agencies.
- Community College – Permits deferrals up to $200 million.
- California State University – permits deferrals up to $250 million.
- Cities and Counties – permits deferrals of specified payments to local governments not to exceed $1 billion.

Through existing administrative authority (no statutory change needed), the Administration could also defer $500 million to the University of California and about $81 million of CalWORKs administrative funding to counties.

Staff Comment: The Department of Finance should explain the need for the cash deferrals in 2011-12 and explain how the 2011-12 plan would compare and contrast to the 2010-11 plan. While cash deferrals to other government units are not desirable, they appear necessary for 2011-12 to avoid payment deferrals to private vendors and taxpayers (such as vendor payments and delayed tax refunds).

Staff Recommendation: Approve the placeholder trailer bill.

Vote:

Issue 2 – Repayment of Special Fund Loans (Governor's Budget)

Governor's Proposal: As indicated in the introduction to this issue, the Governor requests $62 million General Fund to pay interest on outstanding special-fund loans – this is budgeted in item 9620. Interest is only repaid when the loan principal is repaid. The amount of principal repaid is $566 million; however, principal repayment is budgeted as a revenue adjustment instead of an expenditure. The amount of total special fund loans outstanding as of December 31, 2010, is $2.6 billion, according to the Department of Finance. This table below reflects the Administration's planned special-fund loan repayments in 2011-12 (dollars in millions).

Fund Name	Principal	Interest
Accountancy Fund	$10,000,000	$84,521
Contractors' License Fund	10,000,000	727,003
State Dentistry Fund	3,000,000	739,688
Occupational Therapy Fund	640,000	79,627
Enhanced Fleet Modernization Subaccount	20,000,000	169,041
Public School Planning, Design, and Construction Review Revolving Fund	10,000,000	727,003
Housing Rehabilitation Loan Fund	9,200,000	965,526
Rental Housing Construction Fund	500,000	72,762
State Highway Account, State Transportation Fund	200,000,000	19,566,247
Bicycle Transportation Account, State Transportation Fund	6,000,000	586,987
Local Airport Loan Account	7,500,000	733,734
Motor Vehicle Fuel Account, Transportation Tax Fund	8,000,000	782,650
Environmental Enhancement and Mitigation Program Fund	4,400,000	430,457
Historic Property Maintenance Fund	3,000,000	293,494
Pedestrian Safety Account, State Transportation Fund	1,715,000	167,781
Motor Vehicle Account	40,000,000	338,082
Beverage Container Recycle Fund	88,000,000	21,697,524
Tire Recycling Management Fund	27,097,000	2,914,531
Recycling Market Development Revolving Loan Subaccount	1,853,000	248,918
Universal Lifeline Telephone Service Trust Administrative Committee Fund	45,000,000	3,271,512
Deaf and Disabled Telecommunications Program Administrative Committee Fund	30,000,000	2,181,008
Teleconnect Fund	40,000,000	5,373,288
	$565,905,000	**$62,151,384**

Staff Comment: The Department of Finance should present their special-fund loan repayment plan and the LAO should comment. Generally, decisions about special fund loans will be made in the budget Subcommittees by subject-matter area, although the 9620 Budget Item should be made to conform.

Staff Recommendations: Take no action, this is an informational issue.

Senate Budget and Fiscal Review— Mark Leno, Chair

SUBCOMMITTEE NO. 4 Agenda

Senator Michael J. Rubio, Chair
Senator Doug LaMalfa
Senator Noreen Evans

Hearing Outcomes

Thursday, February 3, 2011
9:30 a.m. or upon adjournment of session
Room 112

Consultant: Brian Annis

Item Number and Title **Page**

Proposed Vote-Only Issues:

Proposed Discussion / Vote Issues:

(See Table of Contents on page 1 for a more specific listing of issues)

AGENDA – VOTE ONLY ITEMS

AGENDA – DISCUSSION / VOTE ITEMS

Issues Suggested for Vote Only:

California Tax Credit Allocation Committee (0968)

Department Overview: The mission of the California Tax Credit Allocation Committee (CTCAC) is to fairly allocate federal and state tax credits to create and maintain safe quality affordable rental housing for low-income households in California by forming partnerships with developers, investors, and public entities.

Budget Overview: The Governor's Budget proposes total funding of $5.2 million (no General Fund) and 37.0 positions, an increase of $412,000 and an increase of 2 positions.

Issue 1 – Staff Positions for federal requirements (BCP#1)

Governor's Budget Request: The Administration requests $282,000 (special funds) and the establishment of two new Associate Governmental Program Analyst positions and contract funding for federal reporting related to the Housing and Economic Recovery Act of 2008 and the American Recovery and Reinvestment Act (ARRA) of 2009.

Detail: The CTCAC indicates that the workload relates to new reporting requirements instituted by the federal government on June 23, 2010. Specifically, CTCAC must now obtain "tenant specific data" such as race, ethnicity, age, disability status, income, family composition, use of rental assistance under Section 8, and monthly rental payments for each household member in each tax credit unit in each tax credit project in CTCAC's portfolio of over 3,055 tax credit properties which include 266,417 rental units. Additionally, ARRA requires additional asset monitoring activity. CTCAC cites risk of non-compliance and loss of federal funds if the required reporting is not performed.

Staff Recommendation: Approve the budget request.

Action: Approved request on a 3 – 0 vote.

Issues Suggested for Discussion / Vote:

9210 Local Government Financing

Department Overview: The 9210 budget item includes several programs that include State subventions to local governments for such purposes as health, welfare, and public-safety programs. The public safety funding issues are heard in Subcommittee #5 and constitute most of the budget funding in this item. The topics heard in Subcommittee #4 include interest payments on 2009-10 "Prop 1A" borrowing from local governments – about $90.8 million; and a small subvention to Redevelopment Agencies (RDAs) to help retire a portion of outstanding debt that was backed by the personal property tax – about $500,000. Budget issues related to local government finance, such as shifts or borrowing of local property tax, are also heard under this item.

Budget Overview: The proposed budget for the 9210 item is $551 million General Fund, which is similar to the adjusted 2010-11 level. About $455 million of this amount is related to public safety and heard in Subcommittee #5. The remaining $90 million is heard in Subcommittee #4. Prop 1A interest and RDA personal property tax subventions are ongoing, non-controversial, issues. However, the Governor has proposed a significant budget change this year via the elimination of RDA's –that issue is presented for discussion on the following page.

(See budget issue on next page)

Issue 1 – Elimination of Redevelopment Agencies (Governor's Budget)

Governor's Request: The Governor proposes to eliminate redevelopment agencies (RDAs). This elimination would provide a State General Fund solution of $1.7 billion in 2011-12 by shifting a portion of RDA tax increment to offset General Fund costs for trial courts and Medi-Cal. In 2012-13 and thereafter, the non-obligated portion of RDA tax increment – that revenue not needed for outstanding debt and contractual obligations – would flow instead to K-14 schools, cities, counties, and non-enterprise special districts. To facilitate replacement revenue for local economic development, the Governor proposes to lower the vote threshold to 55 percent for specified local tax increases if the revenue is directed to infrastructure.

Background on Redevelopment: Existing law authorizes cities and counties to create a redevelopment project area to address urban blight. Redevelop and "tax-increment financing," which is bonding against future growth in property tax revenue in an RDA area, have existed in California since the 1950s. RDAs are required to set aside 20 percent of their income to help build affordable housing. The RDA share of property tax revenue has grown substantially from 4 percent in 1983-84 to 12 percent currently and the current level of annual increment revenue is about $5 billion. As the RDA share of property tax has increased, the proportion available for schools and other local governments has decreased. The amount lost to the schools is about $2 billion, and because the State backfills the school revenue, this is an annual General Fund cost of about $2 billion.

Detail on the Governor's Proposal: As indicated, the Governor's proposal would eliminate RDAs. However, because RDA's have outstanding debt service and other contractual obligations, the Governor proposes to create successor entities to administer these obligations. The increment revenue necessary for these outstanding obligations would be directed to these successor entities. The Administration estimates these remain obligations, and existing "pass-through" payments to other local governments would total about $3.3 billion in 2011-12. The remaining $1.9 billion of increment revenue would be allocated $1.7 billion to offset State General Fund costs for trial courts and Medi-Cal, and $210 million to cities and counties. In 2012-13 and thereafter, all the non-obligated increment funds would be directed to schools and local governments, with none directed to State General Fund relief. The K-14 funding would be separate from the Proposition 98 funding calculation, and would be net new revenue for schools. Cities, counties, and non-enterprise special districts would receive new revenue to support their public safety and other functions. The Governor proposes that any existing balances reserved for low and moderate income housing be shifted to local housing authorities for those same purposes.

Proposition 22 and Constitutional Issues: In 2009-10 and 2010-11, a total of $2 billion was shifted from RDA's to local schools using a mechanism that provided the State General Fund with expenditure offsets of the same amount. The California Redevelopment Association was opposed to the 2009-10 and 2010-11 shifts, and was a supporter of Proposition 22, which was approved by voters on the November 2, 2010, ballot. Proposition 22 prohibits the Legislature from enacting statute that would redirect RDA funds to benefit the State. The Governor's plan would eliminate RDAs, and in doing so, the Administration believes the proposal is not in conflict with Proposition 22 or other constitutional provisions.

What the Opponents of the Proposal Say: The California Redevelopment Association in a January 10, 2011, press release indicates redevelopment is a vital local government tool in revitalizing blighted communities and bringing them back to economic vitality by creating jobs, funding affordable housing, building public infrastructure improvements, and creating commercial opportunities. Further, if redevelopment were eliminated, it will have a direct and lasting negative impact on the California economy.

What the Administration Says: The Governor's Budget Summary indicates that the private development that occurs in redevelopment project areas often would have occurred even if the RDAs were never established. While (RDAs) may help relieve localized blight and equalize economic activity related to nearby communities, there are better alternatives for local entities to fund these efforts without shifting resources from schools, counties, special districts, and core city services.

Staff Comment: The Legislative Analyst has prepared a summary of the Governor's proposal. The LAO can present this summary at the hearing and highlight what they think are the key issues for consideration. The Department of Finance will also be available at the hearing to explain the legal and implementation details of the proposal.

Staff Recommendation: Hold open for action in the Full Budget Committee. This issue is a major component of the Governor's budget solution, and should be considered in the full context of the Governor's other expenditure and revenue solutions, and any alternative budget solutions that the Full Budget Committee may wish to consider. Additionally, the Senate Governance and Finance Committee will hear this issue on February 9, and that hearing should result in additional analysis and discussion to further inform the decision on this proposal.

Action: Held open to defer action to full budget committee.

9100 Tax Relief

Department Overview: The 9100 budget item includes several programs that provide property tax relief by making payments to local governments to help defray revenues lost as a result of tax relief programs. There are currently two tax relief programs in this item, and the funding amount indicated is the amount of General Fund proposed for 2011-12:

- Homeowners' Property Tax Relief ($442.2 million)
- Subventions for Open Space / Williamson Act ($1,000)

The Homeowners' Property Tax Relief program is constitutionally required, and therefore is fully funded. The Williamson Act program is a discretionary program and funding has either been eliminated or reduced in recent budget years.

Budget Overview: The estimated funding level for Homeowners' Property Tax Relief is unchanged from the adjusted 2010-11 level of $442.2 million. Williamson Act funding is proposed at $1,000 to suspend state payments. It is budgeted at $1,000 instead of $0 due to a technical budget issue and the need to suspend a continuous appropriation that exists in current statute. Governor Schwarzenegger vetoed program funding to $1,000 in the 2009 Budget Act. A trailer bill to the 2010 Budget Act (SB 863) appropriated $10 million for the program, but the proposed budget would also eliminate this 2010-11 funding. Full funding for the Williamson Act would cost about $40 million.

Issue 1 – Williamson Act Open-Space Funding (Trailer Bill Language)

Governor's Request: The Governor proposes to eliminate the Williamson Act Open-Space subvention payment for both 2010-11 and 2011-12 and scores a General Fund (GF) budget savings of $10 million in each year.

Background: The Williamson Act allows cities and counties to enter into contracts with landowners to restrict certain property to only open space and agricultural uses. The land is restricted in use for 10 or 20 years depending on the type of contract. In return for these restrictions, the property owners pay reduced property taxes because the land is assessed at a lower-than-market level. The State then *partially* compensates the local governments for their related property tax loss. In addition to the direct cost of Williamson Act subventions, the State incurs additional costs from backfilling K-14 schools for their reduced property tax receipts under the Proposition 98 minimum guarantee for K-14 education funding. The following table shows recent funding for Williamson Act by fiscal year (dollars in millions)

Fiscal Year	Prop 98 GF Cost*	Williamson Subvention	Total State GF Cost	Comment
2007-08	$40.0	$37.6	$77.6	Fully Funded
2008-09	$40.0	$33.8	$73.8	10% Cut
2009-10	$40.0	$0	$40.0	Suspended
2010-11 (as enacted)	$40.0	$10	$50.0	Modified Funding Program
2010-11 (proposed)	$40.0	*$0*	*$40.0*	*Suspended*
2011-12 (proposed)	$40.0	*$0*	*$40.0*	*Suspended*

* LAO estimate, actual unknown. Prop 98 education backfill continues in the short run even when the Williamson subvention is suspended. Over the longer run, the Prop 98 backfill cost would fall if counties do not renew contracts.

LAO Comment: The LAO has questioned the cost-effectiveness of the subvention program in prior analyses. The LAO indicates the Governor's proposal warrants approval.

Staff Comment: Suspension of funding does not prohibit land owners and counties from continuing to renew Williamson Act contracts. However, some counties have indicated they will not renew contracts if the state does not provide the subvention.

Staff Recommendation: Hold open for consideration in the full Budget Committee.

Action: Held open to defer action to full budget committee.

Commission on State Mandates (8885)

Department Overview: The Commission on State Mandates (Commission) is responsible for determining whether a new statute, executive order, or regulation contains a reimbursable state mandate on local governments and determining the appropriate reimbursement to local governments from a mandate claim. This budget item appropriates the funding for the staff and operations costs of the Commission, and appropriates non-education mandate payments to local governments. The Constitution, as amended by Proposition 1A of 2004, requires that the Legislature either fund or suspend local mandates – in most cases, if the Legislature fails to fund a mandate, the legal requirements are considered suspended pursuant to the Constitution. Payments for mandate costs incurred prior to 2004 are one exception noted in the Constitution, as are mandates related to labor relations.

Budget Overview: The January Governor's Budget proposed expenditures of \$56.7 million (\$53.7 million General Fund) and 11.0 positions, a decrease of about \$27.9 million over the adjusted current-year budget and no change in positions. It should be noted, the 2010-11 adjusted funding level is after the prior Governor's veto of \$131 million. The Governor's budget includes the continuation of certain mandate suspensions, some new mandate suspensions, and deferrals of mandate payments to generate General Fund savings of about \$321.7 million. The savings measures include: (1) savings of \$94.0 million by deferring payment of pre-2004 mandate claims; (2) savings of \$172.6 million by suspending certain local mandates; and (3) savings of \$55.1 million from deferring payment on expired mandates or some mandates exempt from the requirements of Proposition 1A of 2004. Under (2) above, most mandates are proposed for suspension except those related to law enforcement and tax collection.

Proposed Mandate Funding in Governor's Budget—General Fund

Title	Amount (000s)
Allocation of Property Tax Revenue	596
Crime Victim's Domestic Violence Incident Reports	188
Custody of Minors-Child Abduction and Recovery	13,999
Domestic Violence Arrests and Victim's Assistance	2,565
Domestic Violence Arrest Policies	7,412
Domestic Violence Treatment Services	2,345
Health Benefits for Survivors of Public Safety Officers	1,526
In-Home Support Services II	491
Medical Beneficiary Death Notices	27
Peace Officer Personnel Records	543
Rape Victim Counseling	376
Sexually Violent Predators	21,908
Threats Against Police Officers	40
Unitary Countywide Tax Rates	244
Total	\$52,259

Informational Note: Most of the budget proposals in this area are continuations of budget actions taken over the past few years, such as the deferral in payment of pre-2004 mandate claims. Most mandates have been suspended for multiple years to reduce General Fund costs. The mandates that are presented in this agenda are those that are new proposals or involve new issues. The Governor has proposed to fund one mandate – mental health services for students, or the AB 3632 mandate – within the realignment proposal using Proposition 63 funds. The AB 3632 proposal is being considered by Subcommittee #1.

(See budget issue on next page)

Issue 1 – Elections-Related Mandates

Governor's Request: The Governor proposes suspension of the elections-related mandates for the 2011-12 fiscal year. The Administration estimates this action would result in General Fund savings of about $31 million, although this amount may change after February claims are received. Most of the costs associated with these mandates involve postage and administration costs for absentee ballots, although certain voter-registration procedures are also mandates.

Staff Comment: These elections-related mandates have not been suspended in prior years because there has been concern about how suspension would affect the uniformity of statewide elections. If the mandates are suspended and if individual counties choose to modify their elections procedures, voters could see differential treatment depending on their county of residence.

Staff Recommendation: Keep issue open.

Action: Held open to defer action to full budget committee.

Issue 2 –Brown Act / Open Meeting Mandates

Governor's Request: The Governor proposes suspension of the Brown Act mandates for the 2011-12 fiscal year. The Administration estimates this action would result in General Fund savings of about $63 million, although this amount may change after February claims are received. These mandates require local government to post agendas three-days prior to public hearings and to disclose actions taken in closed sessions. One might think this mandate would be inexpensive – with costs such as the cost of paper, but the state is billed for the time local employees spend drafting such agendas, legal review of the documents, etc.

State Constitution Requires Open Government: Proposition 59 of 2004, amended Article I, Section 3 of the California Constitution to state that the people have the right of access to information concerning the conduct of the people's business, and therefore, the meetings of public bodies and the writings of public officials and agencies shall be open to public scrutiny. Voter-approved mandates do not require state reimbursement, but due to difference in specificity between statute and the Constitution, the reimbursement is currently considered required.

Options to Protect Open Meetings, but Save State Costs: Last year, the Budget Conference Committee adopted trailer bill language that would repeal and reenact relevant provisions of the Brown Act to be best practices for compliance with Proposition 59. This action was thought to be a mechanism to relieve the state's reimbursement requirement but still maintain the current open government practices. That provision was stripped from final trailer bill language as the measure moved to a final vote, because opposition came forward with the fear that the statutory revisions would not be sufficient to maintain open-meeting practices. Another option to relieve state costs in the future would be to amend the Constitution to add specificity. For example, Senate Constitution Amendment (SCA) 7 (Yee), would add this sentence to the Constitution: *Each public body shall provide public notice of its meetings and shall publicly disclose any action taken*.

Current Status of the Brown Act: The Department of Finance has stated that the Brown Act is suspended for 2010-11. While the 2010 budget bill did not list the Brown Act as suspended, it also did not list the Brown Act as funded – this was consistent with the original "best-practices" trailer bill approach. Staff is not aware of any local agencies that have changed their open meeting practices due to the current status of the mandate.

Staff Comment: It is clear from budget hearings over the past few years that the Legislature does not want to diminish open meeting requirements. Efforts have focused on retaining these practices while relieving the state cost of reimbursement. Due to ongoing General Fund pressures and a $63 million cost in 2011-12, a Constitutional amendment may be a good solution for consideration.

Staff Recommendation: Keep issue open.

Action: Held open to defer action to full budget committee.

0520 Secretary for Business, Transportation and Housing

Department Overview: The Secretary of the Business, Transportation and Housing Agency (BT&H Agency) is a member of the Governor's Cabinet and oversees 16 departments, including the following large departments:

- Alcoholic Beverage Control
- Corporations
- Housing and Community Development
- California Highway Patrol
- Motor Vehicles
- Financial Institutions
- Real Estate
- Managed Health Care
- Transportation

In addition, the Secretary's Office oversees programs, including the following, which are budgeted directly in the Secretary's Office:

- Infrastructure and Economic Development Bank
- Film Commission
- Small Business Loan Guarantee Program
- Tourism Commission

Budget Overview: The Governor proposes total expenditures of $100.9 million ($4.2 million General Fund) and 60.7 positions for the Office of the Secretary – an increase of $78.2 million from the adjusted 2010-11 budget, and an increase of 1.5 funded positions. The primary reason for the year-over-year change is a one-time federal grant of $84.4 million to support the Small Business Loan Guarantee Program.

(See budget issue on next page)

Issue 1 – Small Business Loan Guarantee Program Expansion (BCP #2)

Governor's Budget Request. The Governor requests various budget changes related to a federal grant award that will result in one-time funding of $84.4 million for the Small Business Loan Guarantee Program (SBLG). This represents a significant expansion of the program which has typically had a trust-fund balance between $30 million and $40 million. The SBLG Program provides assistance to small businesses that may not qualify for traditional loans, by guaranteeing a portion of the loaned amount. The Administration requests to revert $20 million in General Fund support provided to the program one-time as part of the 2010 Budget Act (AB 1632, Chapter 731, Statutes of 2010). Finally, the Administration requests to double program staff from 1.5 positions to 3.0 positions.

Background / Detail. The Small Business Loan Guarantee Program is administered by 11 non-profit Financial Development Corporations (FDCs) via contracts with the State. In the current year, administration funding for the FDCs sum about $2.2 million ($1.7 million General Fund and $500,000 interest earnings) and the cost of the state oversight positions is about $150,000 (General Fund). The FDCs additionally charge fees in the range of 1 – 3 percent on the loan guarantees – which, with the federal money, could provide administration funding of the magnitude of $5 million depending on the volume of guarantees. The trust fund itself currently has a balance of about $44 million, and loan guarantees must not exceed five times the balance of the trust fund. In recent years, the SBLG Program has experienced significant fluctuation in General Fund support, trust fund earnings, and even a temporary suspension in new loan activities due to a prior reversion to the General Fund. However, the $84 million in federal funds would support the program at a new peak level.

Staff Comment: The federal funds allow the state to expand this program, which is popular in many communities, and at the same time realize a General Fund benefit of $20 million by reverting the augmentation provided last year. This baseline proposal appears to be a "win-win" for the program and State General Fund. The budget question that may merit consideration of the Subcommittee is what level of staffing is appropriate, and can additional General Fund relief be realized from substituting these new federal funds for base program funding and trust fund balances. Specifically:

- Can the state perform program oversight with fewer than 3.0 positions?
- Can the base $1.9 million General Fund support for state administration and the FDCs, be reduced or deleted and backfilled with federal funds?
- Can the base trust fund balance of $24 million be reverted to the General Fund immediately, or over time, and backfilled with federal funds?

LAO Recommendation: The Analyst recommends the Legislature:
a) Adopt the Governor's proposal to revert $20 million to the General Fund.

b) Adopt trailer bill language to allow for the reversion of the additional General Fund dollars as the lines of credit and loans backed by roughly $24 million in state funds expire.
c) Reduce the request for additional staff by one and approve the 0.5 managerial position.
d) Consider eliminating the $1.7 million General Fund subsidy provided to FDCs.

Staff Recommendation:

a) Adopt the Governor's proposal (and LAO recommendation) to revert $20 million to the General Fund.
b) Reject LAO recommendation to adopt TBL to revert base trust fund assets to the General Fund, but adopt TBL to direct that new loan guarantees and renewed loan guarantees use federal funds first – as constrained by any federal rules.
c) Adopt the LAO recommendation to approve 0.5 new staff instead of 1.5 new staff.
d) Reject LAO recommendation to elimination General Fund support for administration, and rather convert program administration funding to 20-percent General Fund and trust fund interest, and 80-percent federal funds, which is proportional to new program resources (trust fund balances should be sufficient to result in no General Fund cost for 2011-12, for a General Fund expenditure savings of about $1.9 million).

Action: Held open to defer action to the February 10 Subcommittee hearing.

8880 Financial Information System for California

Department Overview: The Financial Information System for California (FI$Cal), is an Enterprise Resource Planning (ERP) information technology (IT) project intended to replace, consolidate, and upgrade multiple legacy financial systems with a single system that would encompass the areas of: budgeting; accounting; procurement; cash management; and financial management. The development of FI$Cal resides with four “Partner Agencies,” the Department of Finance, the State Treasurer's Office, the State Controller's Office, and the Department of General Services. The FI$Cal system will be implemented in several phases, or “waves,” over the next decade. Budget Control Section 8.88 is a technical fiscal provision that directs special funds to the FI$Cal project and it will be made to conform to the final budget adopted under the 8880 budget items.

Budget Overview: The Governor proposes $70.8 million ($20.9 million General Fund) for continuing the FI$Cal project. This represents a year-over-year increase of $29.0 million ($5.2 million General Fund). Funded positions would grow from 62.1 to 95.9. The reason for the funding increase is that the project would be moving into the implementation stage with contract award to the vendor by December 31, 2011. The 12-year cost of fully implementing the project is estimated at $1.6 billion (both General Fund and other funds). The Administration is exploring financing options such as bonding and vender-financing to spread costs over a longer period.

(See budget issue on next page)

Issue 1 – FI$Cal Budget Request for 2011-12 (BCP #1)

Governor's Budget Request: As indicated above, the Governor requests $70.8 million ($20.9 million General Fund) for the project in 2011-12. The next 12 months are a critical time for the project, with key decision points on whether to move forward with the project as currently configured, how to finance the project, and to which vendor to award the integration contract. Current law (Government Code 15849.21) requires a report to the Legislature and 90-day review by the Joint Legislature Budget Committee (JLBC), after a contract is negotiated with the winning bidder, but prior to contract award – this report is anticipated in the July – September period of this year.

Project Timeline: Currently, three selected vendors are completing the "Fit-Gap," or stage I contract, which involves a review of potential gaps between the vendor's software and the state's business requirements. Project staff have also ask the three vendor's to propose financing options and held discussion with the State Infrastructure Bank (I-Bank) on financing options. The following are key upcoming dates:

- February 2011 – Financing proposals due from vendors.
- March 2011 – Fit-Gap or Stage I proposals due and begin negotiations.
- July 2011 – Select winning contractor and proceed on final negotiations.
- August 2011 – Deliver Special Project Report #4 and report to JLBC. The JLBC report is required to include costs and benefits of alternative approaches to the implementation of the FI$Cal system, including, but not limited to, a scaled-back version of the system.
- December 2011 (or earlier) – Award contract.
- January 2012 – Ramp up project and costs - $20 million for contractor, $12.7 for State Office of Technology Service, hire 33 new positions, and other activities included in the BCP.

Staff Comments: As the timeline above indicates, there will be new information and legislative reporting coming over the next few months and in the late summer / early fall. Some of this information will be available as the Subcommittee continues with budget hearings in April and May. Other information will only come after the budget is passed and the new fiscal year begins July 1. Due to this schedule, the Subcommittee may wish to consider holding final action on the FI$Cal budget until later this spring. Because the report to the Legislature will not arrive until after the budget is passed, the Legislature will want to carefully consider budget bill language, or trailer bill language, to maintain appropriate legislative funding control after the proposed-contract detail is provided.

Staff Recommendation: Hold open for future consideration in the spring after further detail is available on alternative financing options.

Action: Held open to defer action to the February 10 Subcommittee hearing.

California Alternative Energy and Advanced Transportation Financing Authority (0971)

Department Overview: The mission of the California Alternative Energy and Advanced Transportation Financing Authority (CAEATFA) is to promote the prompt and efficient development of energy sources which are renewable or which more efficiently utilize and conserve scarce energy resources.

Budget Overview: The January Governor's Budget proposed total funding of $25.8 million (special funds and reimbursements) and 7.0 positions, an increase of $9.2 million and no change in positions. The year-over-year increase is primarily explained by the implementation of California Ethanol Producers Incentive Program (See Issue 1 on the following page for detail on this budget request).

Informational Note on the PACE Program: Due to a continuous appropriation enacted last year, the CAEATFA budget includes a $15 million transfer from the Renewable Resource Trust Fund related to the Property Assessed Clean Energy Program (PACE). The PACE Program provides up-front financing for renewable and energy efficiency-related upgrades to properties with a unique financing mechanism of a loan that is backed by the property and transferable to new owners if the property changes hands. Recent state legislation, SB 77 (Chapter 15, Statutes of 2010, Pavley), facilitated program participation by small local governments by allowing them to pool PACE bonds via CAEATFA before going to market. The federal government has recently determined that the PACE program presents significant safety and soundness concerns that must be addressed by Fannie Mae, Freddie Mac, and the Federal Home Loan Banks. The federal action effectively halted the operation of PACE programs while the legal issues now proceed to the courts. The Legislative Analyst recommends the Legislature reverse the $15 million transfer, without prejudice, pending legal resolution of the issue that has suspended PACE activity. Staff suggests no action at this time, as the PACE issue may be addressed in a policy bill, or may be better informed by review in Budget Subcommittee #2 which oversees energy-related budget issues. This Subcommittee can revisit this issue at a later date as warranted.

(See budget issue on next page)

Issue 1 – AB 118 / Ethanol Producers Incentive Program (BCP#1)

Governor's Request: The Administration requests $9 million in reimbursement authority for CAEATFA to receive funds from the California Energy Commission (CEC) to perform activities related to the Alternative and Renewable Fuel and Vehicle Technology Program as authorized by AB 118 (Chapter 750, Statutes of 2007, Nunez). The specific program is the California Ethanol Producer Incentive Program whereby financial assistance is provided to ethanol producers selected by CEC to develop and commercialize advanced transportation technologies that meet advanced energy goals.

Background/Detail: AB 118 authorizes the CEC to implement various programs consistent with the most recently adopted Investment Plan for the Alternative and Renewable Fuel and Vehicle Technology Program. Pursuant to the 2010 Budget Act, CAEATFA and the CEC are entering into an interagency agreement that outlines the terms by which CAEATFA will assist CEC in implementing the ethanol incentive program goals. The interagency agreement is expected to have a 4-year term expiring in January 2015. The terms of the agreement require CEC to transfer a total of $15 million, starting with an initial transfer of $6 million in the current year and $9 million to be transferred once the initial amount is allocated by CAEATFA.

Staff Comment: The Governor's budget requests a $15 million increase in reimbursement and expenditure authority in the current year, and an increase of $9 million in the budget year. The two-year amount requested exceeds the interagency agreement by about $9 million – CAEATFA indicates this is proposed due to uncertainty about how funds will be distributed across fiscal years and to maximize flexibility.

LAO Recommendation: The Legislative Analyst recommends holding action on this item pending receipt of the 2011-12 AB 118 Investment Plan, which should be submitted to the Legislature this March. The Legislature has expressed a great deal of interest in the AB 118 program administered by CEC, and as such, has statutorily required that the CEC annually submit an AB 118 Investment Plan. This requirement is designed to improve the Legislature's oversight of the AB 118 program.

Staff Recommendation: Deny without prejudice to defer final consideration of this request to later this spring after the AB 118 report has been provided and reviewed.

Action: Held open to defer action to the February 10 Subcommittee hearing.

Debt Service General Obligation Bonds and Commercial Paper (9600)

Department Overview: Debt service payments are continuously appropriated, and therefore not appropriated in the annual budget bill. This item in the Governor's Budget displays the estimated debt service costs for each General Obligation bond (GO bond). Some bond costs are offset by special funds or federal funds – primarily by the transportation debt service fund. Other bonds are "self liquidating," or have their own dedicated revenue (i.e., the Economic Recovery Bonds [ERBs] receive a quarter-cent of the sales tax) – the self-liquidating bonds are not included in this item.

Budget Overview: The January Governor's Budget includes $4.9 billion in General Fund costs for GO debt service and related costs. In addition to this amount, $792 million in debt costs are funded from other funds (i.e., $778 million is from the transportation debt fund that is associated with the truck-weight-fee proposal). Finally, federal bond subsidies, through the Build America Bonds (BABs) program, provide $351 million in 2011-12. The table below, with data from the Governor's Budget, shows the three-year GO bond costs (in millions):

	2009-10 Actual Cost	2010-11 Estimated Cost	2011-12 Estimated Cost
General Fund cost	$4,639	$4,890	$4,927
Other funds cost	$239	$644	$792
Federal subsidy (Build America Bond Program)	$155	$300	$351
TOTAL Item 9600	**$5,033**	**$5,834**	**$6,070**
Economic Recovery Bonds (not included above)	$1,566	$1,351	$1,407

According to the Governor's Budget, the State has $79.8 billion in outstanding GO bond debt (including self-liquidating bonds). Another $39.6 billion in bonds is authorized, but unissued. The Governor's proposed budget includes $84.6 billion in General Fund expenditure, so GO bond debt service as a percentage of General Fund expenditures is 5.8 percent (or 7.5 percent when ERBs are included).

(see budget issue on next page)

Issue #1 - Deferral of Spring 2011 Bond Sale (Governor's Proposal)

Governor's Proposal: The Administration proposes to defer the spring 2011 bond sale until the fall, which would result in General Fund debt-service savings of approximately $248 million in 2011-12. During budget hearings last spring, the Schwarzenegger Administration had assumed a spring 2011 bond sale of $6.7 billion, but that number had been revised down to $3.5 billion in the Administration's fall estimate. This is not scored as a General Fund solution in the budget, because the assumption was built into the workload budget. The Administration now assumes $5.8 billion in bond sales this fall.

Detail: There has been some uncertainty among the various bond stakeholders about what the sales deferral means for individual bond programs. The Governor's budget explicitly cites a policy change to decrease Proposition 1C Housing bonds by $99 million in 2011-12 to reflect a one-time pause in new loans and grants for housing projects. Aside from the Proposition 1C statement, the Administration has told Committee staff that the remainder of bond programs should proceed as previously expected with cash balances from prior bond sales. Specifically, a cash balance of $13.3 billion from prior bond sales was on hand in December 2010, and that amount is expected to fund all underway bond projects through December 2011, and fund new project allocation that are planned to occur through June 2011 (including cash for those new projects also through December 2011). For projects expecting an allocation after June 2011, and for ongoing project cash needs after December 2011, the state would need to sell additional bonds this fall. The below table shows cash on hand by bond for some of the major bond acts (dollars in millions).

Bond Program	**Cash, or bond proceeds, as of Dec 2010**
Prop 1B of 2006: Transportation	$3,112
Prop 1E of 2006: Disaster Prep and Flood Prevention	$1,709
Prop 84 of 2006: Safe Drinking Water	$1,565
Prop 46 of 2002 &Prop 1C of 2006: Housing	$1,339
Prop 47 of 2002 & Prop 55 of 2004: Education Facilities	$1,249
Prop 71 of 2004: Stem Cell Research	$361
Prop 3 of 2008: Children's Hospital Bond Act	$341
Prop 1A of 2008: High Speed Rail	$245
All others	$3,406
TOTAL	**$13,327**

Staff Comment: The Administration should outline their plan for bond sales and how it will affect infrastructure projects under construction, and near construction.

Staff Recommendation: Take no action, this is an informational issue.

Action: Information issue, no action taken.

9620 Cash Management and Budgetary Loans

Department Overview: This budget item appropriates funds to pay interest costs on General Fund borrowing used to overcome cash flow imbalances during the fiscal year. Because receipts and disbursements occur unevenly throughout the fiscal year, the General Fund borrows in most years, even though each budget is balanced when enacted and funds are repaid within the fiscal year. Interest is paid on both internal borrowing (such as cashflow loans from special funds) and for external borrowing (such as Revenue Anticipation Notes [RANs]). This item additionally pays interest costs for budgetary borrowing by the General Fund from special funds. Budgetary borrowing is across fiscal years and is scored as a budget solution, whereas cashflow borrowing is not counted as a budget solution (only a cash solution).

Budget Overview: The January Governor's Budget includes $300 million for interest costs on cashflow borrowing and $62 million for interest costs on budgetary borrowing – all General Fund. Of the cashflow amount, $100 million is for internal borrowing and $200 million is for external borrowing. Overall, expenditures in this item are up significantly – a total of $362 million is proposed for 2011-12, versus revised expenditures of $230 million in 2010-11. The year-over-year difference is primarily explained by the late budget last year that delayed the RAN sale until late in 2010. The Administration assumes the 2011-12 RAN sale will occur in July, resulting in a longer borrowing period and higher interest costs.

(see budget issues on next page)

Issue 1 – Intra-year Payment Deferrals / Cashflow Loans (Trailer Bill Language)

Governor's Proposal: The Administration requests statutory change that would allow intra-year cash payment deferrals in 2011-12, which would be similar to the authority granted for 2010-11. These deferrals represent an additional cashflow solution that have been necessary even after internal and external cashflow borrowing. The language also allows cashflow loans from two additional funds: the Immediate and Critical Needs Account in the State Court Facilities Construction Fund, and the Hospital Quality Assurance Revenue Fund.

Background: Last year's cashflow measure were enacted by three bills: AB X8 5; AB X8 14; and AB 1624. The 2010-11 legislation provided approximately $5 billion in cashflow relief, and this year's proposal would be reduced to about $4.5 billion, due to the prohibition placed on borrowing from certain transportation funds by Proposition 22 of 2010. Last year's deferral plan was developed in consultation with higher education and local governments to minimize negative consequences. Finally, the plan includes triggers, such that the deferrals will not occur if the team of the State Treasurer, the State Controller, and the Director of Finance concur they are not necessary to maintain cash balances for the State. Cashflow loans are allowed for most special funds and existing statute requires repayment as needed for the program.

Detail: As indicated above, the Governor's proposal for 2011-12 is very similar to the enacted plan for 2010-11. The following are the major statutory components:

- K-12 Education – Permits up to 3 deferral periods not to exceed $2.5 billion at any one time. Includes a hardship-exemption process for certain local education agencies.
- Community College – Permits deferrals up to $200 million.
- California State University – permits deferrals up to $250 million.
- Cities and Counties – permits deferrals of specified payments to local governments not to exceed $1 billion.

Through existing administrative authority (no statutory change needed), the Administration could also defer $500 million to the University of California and about $81 million of CalWORKs administrative funding to counties.

Staff Comment: The Department of Finance should explain the need for the cash deferrals in 2011-12 and explain how the 2011-12 plan would compare and contrast to the 2010-11 plan. While cash deferrals to other government units are not desirable, they appear necessary for 2011-12 to avoid payment deferrals to private vendors and taxpayers (such as vendor payments and delayed tax refunds).

Staff Recommendation: Approve the placeholder trailer bill.

Action: Held open to defer action to the February 10 Subcommittee hearing.

Issue 2 – Repayment of Special Fund Loans (Governor's Budget)

Governor's Proposal: As indicated in the introduction to this issue, the Governor requests $62 million General Fund to pay interest on outstanding special-fund loans – this is budgeted in item 9620. Interest is only repaid when the loan principal is repaid. The amount of principal repaid is $566 million; however, principal repayment is budgeted as a revenue adjustment instead of an expenditure. The amount of total special fund loans outstanding as of December 31, 2010, is $2.6 billion, according to the Department of Finance. This table below reflects the Administration's planned special-fund loan repayments in 2011-12 (dollars in millions).

Fund Name	Principal	Interest
Accountancy Fund	$10,000,000	$84,521
Contractors' License Fund	10,000,000	727,003
State Dentistry Fund	3,000,000	739,688
Occupational Therapy Fund	640,000	79,627
Enhanced Fleet Modernization Subaccount	20,000,000	169,041
Public School Planning, Design, and Construction Review Revolving Fund	10,000,000	727,003
Housing Rehabilitation Loan Fund	9,200,000	965,526
Rental Housing Construction Fund	500,000	72,762
State Highway Account, State Transportation Fund	200,000,000	19,566,247
Bicycle Transportation Account, State Transportation Fund	6,000,000	586,987
Local Airport Loan Account	7,500,000	733,734
Motor Vehicle Fuel Account, Transportation Tax Fund	8,000,000	782,650
Environmental Enhancement and Mitigation Program Fund	4,400,000	430,457
Historic Property Maintenance Fund	3,000,000	293,494
Pedestrian Safety Account, State Transportation Fund	1,715,000	167,781
Motor Vehicle Account	40,000,000	338,082
Beverage Container Recycle Fund	88,000,000	21,697,524
Tire Recycling Management Fund	27,097,000	2,914,531
Recycling Market Development Revolving Loan Subaccount	1,853,000	248,918
Universal Lifeline Telephone Service Trust Administrative Committee Fund	45,000,000	3,271,512
Deaf and Disabled Telecommunications Program Administrative Committee Fund	30,000,000	2,181,008
Teleconnect Fund	40,000,000	5,373,288
	$565,905,000	**$62,151,384**

Staff Comment: The Department of Finance should present their special-fund loan repayment plan and the LAO should comment. Generally, decisions about special fund loans will be made in the budget Subcommittees by subject-matter area, although the 9620 Budget Item should be made to conform.

Staff Recommendations: Take no action, this is an informational issue.

Action: Informational issue not heard, defer discussion to February 10 Subcommittee hearing.

Senate Budget and Fiscal Review—Mark Leno, Chair

SUBCOMMITTEE NO. 4 Agenda

Senator Michael J. Rubio, Chair
Senator Noreen Evans
Senator Doug LaMalfa

Monday, February 7, 2011
2:30 p.m. or Upon Adjournment of Session
Room 112

Consultant: Kris Kuzmich

PART A

Item Number and Title

0502	California Technology Agency
8855	Bureau of State Audits
8955	California Department of Veterans Affairs

(See Table of Contents on page 2 for a More Specific Listing of Issues)

Pursuant to the Americans with Disabilities Act, individuals who, because of a disability, need special assistance to attend or participate in a Senate Committee hearing, or in connection with other Senate services, may request assistance at the Senate Rules Committee, 1020 N Street, Suite 255 or by calling 916-324-9335. Requests should be made one week in advance whenever possible.

AGENDA – VOTE ONLY ITEMS

(Please see summary chart on Page 3)

AGENDA – DISCUSSION / VOTE ITEMS

Issues Proposed for Vote Only:

	Issue	2011-12 Amount	Fund Source	Staff Recommendation
	California Department of Veterans Affairs (8955)			
1	Yountville Veterans Home: Veterans' Cemetery Renovation	$2.4 million	Federal Funds	APPROVE
2	Yountville Veterans Home: Chilled Water Distribution System	$2.236 million	Lease Revenue Bond Funds	APPROVE
3	Yountville Veterans Home: Steam Distribution System Renovation	$3.387 million	Lease Revenue Bond Funds	APPROVE

Vote:

Issues Proposed for Vote Only – Issue Descriptions

CALIFORNIA DEPARTMENT OF VETERANS AFFAIRS (8955)

For overview and budget information regarding this department, please see page 12 of this agenda.

Issue 1 – Yountville Veterans Home: Veterans' Cemetery Renovation

Governor's Request. The Governor requests $2.4 million (federal funds) for the construction phase of the Yountville Veterans Home cemetery restoration project. General obligation bonds have previously been approved in the amount of $436,000 for the preliminary plans and working drawing phases of the project. The complete project costs total $2.847 million and will be fully reimbursed by the federal government once the grant is awarded.

Background. The cemetery at the Yountville Veterans Homes is the second oldest veterans' cemetery in the nation covering approximately 10.27 acres. The cemetery is reserved for veterans who reside at any CDVA veterans home. The condition of the cemetery over the past several decades has continued to deteriorate and is considered to be in a severe state of disrepair. More specifically, much of the cemetery infrastructure, including the sewage and water distribution systems, need to be repaired and/or replaced. The objectives within this restoration project will bring the cemetery into compliance with the National Cemetery Administration standards and enable the state to maintain the cemetery grounds according to those standards in future years.

Issue 2 – Yountville Veterans Home: Chilled Water Distribution System Renovation

Governor's Capital Outlay Request. The Governor requests $2.236 million (lease revenue bonds) to correct system deficiencies in the Chilled Water System at the Yountville Veterans Home. The additional chiller plant and replacement of cooling towers, pumps, and valves will ensure the Yountville Home has the required chiller capacity to maintain a proper temperature throughout the Home to protect the health and safety of the elderly and/or disabled veteran residents. The total estimated project cost is $6.398 million and will be funded by: (1) $497,000 – Veterans' Home Bond; (2) $2.236 million – Lease Revenue Bonds; and (3) $3.665 million – Federal Trust Fund.

Background. The chilled water system at the Yountville Home does not maintain the water at the proper temperature when the outside air temperature exceeds 96°F. As a result, patient areas exceed temperature limits mandated by the California Department of Health Services. Due to other system deficiencies (e.g., cooling towers, pumps, and valves), additional capacity solely on its own will not allow the cooling system to efficiently and effectively meet the increased demand on the chilled water cooling system. The project will renovate the chilled water system by adding chiller capacity and replacing cooling towers, chilled water pumps, condenser water pumps, automatic flow control valves, automatic water isolation valves, and bypass circuit and automatic valves. A new

400 ton chilled water system will be installed adjacent to Holderman Hospital along with a 400 kW generator to provide emergency/back-up power.

Issue 3 – Yountville Veterans Home: Steam Distribution System Renovation

Governor's Capital Outlay Request. The Governor requests $3.387 million (lease revenue bonds) to renovate the deteriorating underground steam distribution system at the Yountville Veterans Home. The project includes replacement of underground lines and valves and removal and replacement of badly deteriorated asbestos insulation that is a safety hazard. As part of landscaping an area disrupted by the steam lime replacement project, 10 ADA-accessible parking spaces will be provided to an underserved part of the Home. The total estimated project cost is $7.482 million and will be funded by: (1) $3.387 – Lease Revenue Bonds; and (2) $4.095 million – Federal Trust Fund.

Background. Steam provides heating and domestic hot water to all 120 buildings that serve the elderly and disabled veterans who reside at the Yountville Home. Steam is also instrumental in preparation of food for all residents. Furthermore, steam is used to keep the food warm to be served in the seven dining rooms used by residents or by bedside services. Last, steam is used by the heat exchanger to provide cooling for the buildings and residential areas. The steam lines are currently insulated using asbestos containing material and are badly deteriorated. As a result, loose asbestos containing material is present in several manhole accesses throughout the facility.

This project will also add 10 ADA-accessible parking spots to the Section A residence. This residence currently houses 90 members, but only has 12 parking spaces. Because the steam line renovation will disturb the landscaping adjacent to the residence, it is cost effective to fold the additional parking spaces into this project. A stand-alone parking project of this size would be unable to garner federal participation.

Renovation of the steam distribution system will ensure a safer and more energy efficient operation and the uninterrupted availability of steam for the Yountville Home's critical daily operations.

0502 CALIFORNIA TECHNOLOGY AGENCY

Department Overview. The California Technology Agency (CaTA) establishes and enforces statewide information technology (IT) strategic plans, policies, standards, and enterprise architecture, and oversees IT projects and public safety emergency communications systems for all state departments. Effective January 2, 2011, Chapter 404, Statutes of 2010 (AB 2408), renamed the Office of the State Chief Information Officer the "California Technology Agency" and codified the statewide IT consolidation originally implemented by the Governor's Reorganization Plan No. 1 in 2009.

The Officer of Technology Services (OTech) within CaTA, provides the IT processing platforms for over 500 customers, including the Executive Branch and public entities. OTech is accountable to its customers for providing secure services that are responsive to their needs and represent best value to the state. The OTech is a fee-for-service organization and operates as a 100 percent reimbursable department. OTech's Service Level Agreements (SLAs) with its customers include a 99.9 percent service availability goal for IT services. The OTech must continue to provide sufficient processing capacity to deliver the performance and service agreed to in the SLAs.

Budget Overview. The January Governor's Budget provides 1,364.2 authorized positions and $486.2 million ($3.7 million GF). The increased funding primarily reflects additional expenditure authority associated with increased computer system utilization at the state level, including mainframe processing, data storage, and server capacity.

Issues Proposed for Discussion / Vote

Issue 1 – Mainframe Processing Capacity, Database Hosting, Data Storage, and Email Hosting

Governor's Budget Request. The Governor requests total increased expenditure authority of $29.7 million (Technology Services Revolving Fund) and 23 positions. The increased expenditure authority is associated with increased computer system utilization at the state level, including mainframe processing, data storage, and server capacity, as illustrated in the below chart. Note, each item is described in detail beginning on the next page. The fund source for all items is the Technology Services Revolving Fund.

	2010-11 Funding Level	Description	Positions
Mainframe CPU Processing	$5.499 million	1.616 million of Instructions Per Second (MIP)	
Midrange Server	$8.186 million ($2.044 ongoing)	95 addition UNIX server instances and 412 additional Windows server instances	20.0
Data Storage Capacity	$5.366 million	Hardware, software, and connectivity components	
CA.mail and California Email Services	$10.639 million	Implement vendor hosted California Email Services	3.0

Mainframe CPU Processing

The CaTA, on behalf of the OTech, requests increased expenditure authority of $5.499 million (Technology Services Revolving Fund) in 2011-12 for the purchase of mainframe processing capacity [1.616 million of Instructions Per Second (MIPS)] to accommodate existing and projected increases in workload resulting from customer program growth and program changes. Costs included in this request are based on current pricing for this type of upgrade, plus the costs of supporting the components. Of OTech's current total of 500 customers, approximately 250 are mainframe processing customers. New state anti-fraud initiatives, federal reporting requirements, and natural population and caseload growth have driven a projected 14 percent increase in mainframe transactions for 2011-12. OTech's capacity must increase to provide sufficient resources for customer workloads because OTech acquires processing capacity only as needed for current workloads; i.e., the projected growth cannot be absorbed into the existing computing infrastructure.

Midrange Server

The CaTA, on behalf of OTech, requests increased expenditure authority of $8.186 million (Technology Services Revolving Fund) in 2011-12 to: (1) purchase 95 additional UNIX server instances and 412 additional Windows server instances for growth; (2) replace 25 UNIX servers and 50 replacement Windows server instances; and (3) add 20.0 permanent staff for the support of server instances, databases, and web services. Of the total funding requested, one-time costs are $6.142 million for the UNIX and Windows server instances and software cost and ongoing costs are $2.044 million for the 20 additional positions. OTech's processing capacity must continue to increase to meet the ever growing IT demands of its 500 customers. Governmental programs increase their reliance on technology to meet growing program workload with greater efficiency. This saves the taxpayer funds overall, but results in a continual increase in: (1) the number of installed servers at OTech; (2) related refresh/replacement of servers; and (3) tasks needed to provide support services for this growth.

Data Storage Capacity

The CaTA, on behalf of the OTech, requests increased expenditure authority of $5.366 million (Technology Services Revolving Fund) in 2011-12 for hardware, software, and connectivity components to ensure adequate data storage support to meet needs of customer driven workloads. Without capacity upgrades and growth, OTech will be unable to support the growth of customer programs, the systems will reach capacity, and customers will be unable to add new data.

CA.mail and California Email Services

The CaTA, on behalf of the OTech, requests increased expenditure authority of $10.639 million (Technology Services Revolving Fund) in 2011-12 and three positions to implement the vendor hosted California Email Services (CES). The increased expenditure reflects the requirement in Executive Order S-03-10, and statutorily in Chapter 404, that all executive branch agencies are required to migrate to either the OTech operated CA.mail or the third party hosted CES by June 2011. The migration will improve security and standardization of IT across State government.

CaTA Prior Year Project Adjustments

The Governor requests prior year baseline adjustments for the CaTA's expenditure authority to align previously approved budget actions with the ongoing costs of the related projects. The adjustments result in a net reduction of $10.2 million (Technology Services Revolving Fund) in 2010-11 and $10.0 million (Technology Services Revolving Fund) in 2011-12. The purpose of these adjustments is to align the OTech budget with actual expenditures in order to maintain a connection between spending authority level of OTech and the actual expenditures required to support the needs of its customers.

Staff Comment. These requests are consistent with the consolidation of IT within the CaTA, which the Legislature approved in 2009 with the adoption of the Governor's Reorganization Plan No. 1. The CaTA, and OTech more specifically, must continue to provide sufficient computing capacity to deliver performance and service to its customers. These requests are integral to OTech meeting that charge and providing its customers with the agreed upon service levels.

Staff Recommendation: Approve the budget requests.

Vote:

Issue 2 – Independent Project Oversight

Governor's Budget Request. The Governor requests $966,000 (Technology Services Revolving Fund) and nine permanent positions for Independent Information Technology Project Oversight (IPO) in 2011-12 and ongoing to meet workload increases and mandated responsibilities of Chapters 183 and 404, Statutes of 2007 (SB 90) and Statutes of 2010 (AB 2408), respectively, and to ensure consistent project implementation of the state's IT projects.

Background. The increased expenditure authority in this request is for a staffing expansion that the CaTA considers a critical priority due to legislative mandates, increased public visibility, and the need to ensure consistent project implementation of the state's IT projects. These positions would provide independent project management services to customer departments. The costs associated with the IT project management will be funded by the agency or department administering the project. The CaTA would be reimbursed 100 percent by the department or agency requesting the services. Once the CaTA has created a professional state governmental entity, comprised of state staff, to manage and direct IT policy, standards, and projects, the state's current reliance on high paid contractors will be diminished. The state currently spends approximately $17.2 million annually on contracted IT project oversight and management.

Staff Comment. The proposed positions represent the beginning of the implementation of CaTA's expanded role as outlined in Chapter 404. Staff concurs that having IPO conducted in-house (as opposed to contracted out) will save the state as the state will no longer rely on highly paid contractors and will instead develop a cadre of IT professionals within state service. However, in considering this request, the Subcommittee may wish to defer action until later in the Spring so that all factors and the CaTA's resources can be considered at one time.

Staff Recommendation: Deny the budget request without prejudice and consider as part of the Spring 2011 budget process.

Vote:

8855 BUREAU OF STATE AUDITS

Department Overview. The California State Auditor (Auditor) promotes the effective and efficient administration and management of public funds and programs by providing citizens and government nonpartisan, accurate, and objective assessments of state and local governments' financial and operational activities. As the independent auditor, the Auditor is the only state entity that the law grants full access to all records of state and local agencies, special districts, school districts, and any publicly created entity.

The Auditor conducts: (1) performance, financial, or compliance audits that are either mandated by statute or requested by the Legislature through the Joint Legislative Audit Committee (JLAC); (2) California's Single Audit, a combination of the independent audit of the State's basic financial statements and the independent audit of numerous federal programs administered by the State, which is required as a condition for the state to receive billions in federal funds each year; and (3) evaluations of those issues and entities identified as being high risk. Statutorily-required audits are the first priority for the Auditor, followed by those approved by the JLAC, and then those audits conducted under the Auditor's high-risk authority.

Finally, under the California Whistleblower Protection Act, the Auditor has broad authority to perform independent investigations into complaints that state employees or agencies have engaged in improper conduct. Additionally, the Auditor administers California's Whistleblower Hotline that enables the public to report improper acts committed by state agencies, departments, or employees.

Budget Overview. The January Governor's Budget provides $24.8 million ($14.0 million GF) and 181 positions. This is an increase of $8.2 million ($4.7 million GF) and 34 positions. Year-to-year, the Auditor's Budget shows only a net increase of $5.5 million, but this is due to a reduction in contract audit work and American Recovery and Reinvestment Act audit and oversight work.

Issue Proposed for Discussion / Vote:

Issue 1 – Budget Augmentation

Governor's Budget Request. The State Auditor requests an increase of $8.2 million ($4.7 million GF) and 34 positions in 2011-12 to fund a two-year plan to better assist the Legislature in its oversight of government operations, including conducting additional audits, completing more high risk analyses, and better integrating the audit process with the work of legislative budget and policy committees.

Background. The State Auditor requests the increased funding as part of a two-year plan to better assist the Legislature in its oversight of government operations. Currently, the Auditor has 147 staff. In Year 1 of this plan, the Auditor proposes to increase staffing by 34 positions, to a total of 181 positions. In Year 2, an additional 37 staff would be added, bringing staffing to a total of 218 positions. The following chart illustrates this two-year staffing plan:

Staffing Categories	Current Level 2010-11	Year One 2011-12	Year Two 2012-13	Total
Audit	93	28	26	147
Investigative	9	3	5	17
Information Technology	6	2	2	10
Executive Office	6	1	2	9
Legal	4	0	2	6
Administration/Support	29	0	0	29*

**The support staff number may grow slightly during the two-year plan; if so, the number of audit positions would be decreased by a like amount.*

In Year 1, the Auditor reports that it will utilize $3.5 million of the requested funding to contract with outside experts to conduct the federal compliance audit work, thereby allowing the Auditor to utilize the remaining $4.5 million to recruit, hire, and train the 34 new in-house staff to conduct the additional mandated, discretionary, and high-risk audit work as well as investigations. These 34 staff will also respond to increases in other activities, such as inquiries and requests from legislative staff, legal assistance, and public record requests, due to the additional audits being completed.

In Year 2, the Auditor reports that it should have a sufficient number of trained audit and investigative staff to conduct the increase in audit work and provide the additional integration with legislative oversight. Consequently, in Year 2, the Auditor plans to substantially reduce or eliminate the contracted federal compliance work to hire the additional 37 staff.

At the end of the two-year plan, which will result in the addition of 54 new audit staff, the Auditor reports that audit production will increase from the 2010-11 average of 30 per year, to 50-55 per year, including discretionary and mandated audits, as well as more work under the high-risk authority. The additional audit staff will also reduce the time it currently takes to complete an audit, and will also reduce staff burnout and a high turnover rate. The Auditor reports that the addition of eight investigative staff over the two years will result in self-initiated statewide investigations increasing from the 2010-11 average of one per year to four to eight per year.

Chapter 160, Statutes of 2010 (AB 1749), extends the protections under the California Whistleblower Protection Act to employees of the Judicial Branch. The Auditor indicates that the expansion of its Investigative Unit under the two-year plan is due in part to the expected increase in Whistleblower activity resulting from this change in law.

The Auditor indicates that the additional audit and investigative results from the two-year plan will produce more monetary benefits for the state, and offers the following recent examples of savings from audit and investigative work: (1) $194 million in unallowable costs, plus $53 million in cost avoidance over seven years (State Mandates Audits, 2003 and 2009); (2) $3.3 million revenue increase (Citation Penalty Accounts, 2010-108); (3) $4.8 million in cost avoidance (Medi-Cal TARS, 2009-112); and (4) $12 million cost recovery (CalWorks, 2009-101)

Staff Recommendation: Approve the budget request.

Vote:

8955 CALIFORNIA DEPARTMENT OF VETERANS AFFAIRS

Department Overview. The California Department of Veterans Affairs (CDVA) promotes and delivers benefits to California veterans and their families. More specifically, the CDVA provides: (1) California veterans and their families with aid and assistance in presenting their claims for veterans' benefits under the laws of the United States; (2) California veterans with beneficial opportunities through direct low-cost loans to acquire farms and homes; and (3) the state's aged and disabled veterans with rehabilitative, residential, and medical care and services in a home-like environment at the Veterans Homes of California (VHCs). The CDVA operates VHCs in Yountville (Napa County), Barstow (San Bernardino County), Chula Vista (San Diego County), and Greater Los Angeles Ventura County (with homes in West Los Angeles, Ventura, and Lancaster).

Budget Overview. The January Governor's Budget proposes to continue to ramp-up admissions at the VHCs in West Los Angeles, Lancaster, and Ventura. The Governor also proposes to provide continued resources and staffing related to the construction and activation of two new VHCs, in Redding and Fresno, both of which are scheduled to begin admissions in early calendar year 2012. The January Governor's Budget provides CDVA with 2,396.5 authorized positions and $399.3 million ($253.4 million GF).

The construction cost of the VHCs was/is funded with $50 million in general obligation bonds available through Proposition 16 (2000), an estimated $212 million in lease-revenue bonds [most recently amended by Chapter 824, Statutes of 2004 (AB 1077)], and federal funds.

Issues Proposed for Discussion / Vote:

Issue 1 – Program 30, Veterans Homes of California

Governor's Request. The Governor requests a net GF increase of $39.8 million in 2011-12 for all of the VHCs, including: (1) an augmentation of $32.1 million for full-year and one-time adjustments to phase-in staffing and residents in the existing and new VHCs in Greater Los Angeles Ventura County (GLAVC), Redding, and Fresno; (2) $4.7 million for furlough and personal leave program reductions which are only reflected in the 2010-11 fiscal year budget; and (3) $9.3 million in increased lease-revenue bond payments for VHC-GLAVC. The expenditures are offset by an increase of $5.8 million in GF revenue.

2010-11 Budget. The 2010-11 budget provided the following for the VHCs: (1) VHC-GLAVC, 101.3 positions and $7.5 million GF to continue construction, activate business, and begin admitting veterans; and (2) VHC-Redding and VHC-Fresno, respectively, 9.3 positions and $908,000 GF, and 8.5 positions and $908,000 GF, for Construction Completion and Pre-Activation Phase II activities.

Background. The CDVA provides residential and medical care services to honorably discharged California veterans who served on active duty and are over the age of 62 or disabled. The VHCs are long-term residential care facilities that provide California's qualified aged or disabled veterans with rehabilitative, residential, medical, and support services in a home-like environment. Once an eligible veteran selects a VHC as his or her long-term care option, and is approved for admission, the veteran becomes a fee paying resident of the VHC. Home residents are veterans of military service ranging from World War II, Korea, Vietnam, Gulf War I, and Operation Enduring Freedom and Operation Iraqi Freedom. Spouses of veterans may also be eligible for VHC membership. The VHCs provide a long-term continuum of care, from domiciliary care at one end of the spectrum, which is similar to independent living accommodations, to skilled nursing care at the other end of the spectrum, which provides continuous skilled nursing or rehabilitation services. The chart below illustrates the six VHCs that are currently operating, including their licensed bed capacity and levels of care provided:

Veterans Homes of California

	Yountville	**Barstow**	**Chula Vista**	**West Los Angeles**	**Lancaster**	**Ventura**
Year Established	1884	1996	2000	November 2010	February 2010	January 2010
Licensed Beds*	1,207	344	400	84	60	60
Domiciliary Care	Yes	Yes	Yes	No	No	No
Residential Care Facility for the Elderly	Yes	No****	Yes	Yes	Yes	Yes
Intermediate Care Facility	Yes	Yes	No	No	No	No
Skilled Nursing Care	Yes	Yes	Yes	Yes***	No**	No**
Memory Care	Yes	Yes	Yes	Yes	No	No

**Includes suspended beds.*
***Residents needing SNF care at VHC-Ventura or VHC-Lancaster will transfer to VHC-West Los Angeles.*
****To be added in 2011-12.*
*****Barstow is not currently licensed or budgeted for the Residential Care Facility for the Elderly level of care.*

The VHC-Redding and VHC-Fresno facilities are scheduled to open in early calendar year 2012. Both of these homes will provide the following levels of care: Residential Care Facility for the Elderly and Skilled Nursing Care, including Memory Care services within each level of care.

Staff Comment. Staff agrees with the need to adequately and appropriately staff the VHC-GLAVC facilities, as well as VHC-Redding and VHC-Fresno. CDVA indicates that the hiring and occupancy timeframes have been updated to reflect admission schedules and level-of-care offerings at these homes. Further, CDVA indicates that it utilizes a “point-in-time” hiring approach, where staff is added as resident admissions increase. However, it is worth noting that in past years when this Subcommittee considered similar VHC requests, and after the May Revision when caseloads are updated, some salary savings have been found because not all of the positions contained in the requests would be hired per the updated schedules.

Staff also notes that some questions have arisen about veteran demand at the GLAVC facilities. More specifically, both VHC-Lancaster and VHC-Ventura have been open since January and February 2010, respectively. Both homes were scheduled to admit eight residents per month for the first three months and then five residents each month thereafter until their budgeted capacity of 54 was reached in August and September 2010, respectively. As of January 17, 2011, VHC-Lancaster had 22 residents; VHC-Ventura had 39 residents. VHC-West Los Angeles opened in October 2010. It is scheduled to admit eight residents per month for the first three months and then five residents each month thereafter until it reaches its budgeted capacity of 39 as of July 2011. As of January 17, 2011, VHC-West Los Angeles had 21 residents.

The CDVA indicates that both VHC-West Los Angeles and VHC-Ventura are on track to reach their census goal of 39 and 54 respectively by the end of the 2010-11 fiscal year; for VHC-Ventura, this is ten months longer than the original schedule. In the case of VHC-Lancaster, CDVA indicates that the home may not reach its goal. The CDVA indicates that there is presently a lack of demand and applications for VHC-Lancaster; the CDVA indicates that it is engaged in a focused marketing and outreach campaign to reverse the situation. Regardless, given the current resident census at the GLAVC facilities, staff notes that there will likely be salary savings in the 2010-11 budget due to the pace of admissions and admission levels at both VHC-Ventura and VHC-Lancaster. Staff does not recommend making any current year adjustments, as five months remain in the 2010-11 year and any savings will revert to the GF automatically. However, this situation presents a challenge for the Subcommittee in its consideration of the 2011-12 request for VHC-GLAVC, as well as for VHC-Redding and VHC-Fresno.

Given the expedited timeframe for adoption of the 2010-11 budget, it will not be possible to know now what budget adjustments might need to be made to the VHC caseloads and budget post the May Revision, including if the situation at VHC-Lancaster does not reverse itself. However, it is known that some portion of the resources contained in this request will be needed at the GLAVC, Redding, and Fresno VHCs. Therefore, while staff recommends approval of this request, staff also recommends the Subcommittee clearly state its intent to reopen the VHC budget in Spring 2011 when caseloads are better known to make necessary adjustments to the 2011-12 budget.

Staff Recommendation: Approve the budget request but state intent to reopen the Veterans Home of California budget in Spring 2011 when caseloads are known and to make any necessary adjustments to the 2011-12 budget.

Vote:

Issue 2 – County Veterans Service Offices / Operation Welcome Home

Governor's Budget Request. The Governor requests to eliminate $9.9 million GF ($7.6 million local assistance and $2.3 million state operations) support for County Veterans Service Offices (CVSOs) and Operation Welcome Home (OWH) in 2011-12.

2010-11 Budget. The 2010-11 Budget provided baseline funding of $2.6 million GF and $544,000 (Veterans Service Office Fund - VSOF) to counties for CVSOs. The $2.6 million GF figure has been static since 2004. In addition, the 2010-11 Budget provided new funding to implement and sustain OWH as follows: (1) $5 million GF in ongoing operations funding for CVSOs, Veterans Service Organizations, and Non-Profit Organizations that provide services to veterans; and (2) a one-time VSOF augmentation of $768,000 to be spent over three years to implement the Subvention Administrative Information System, a common veteran case management application in CVSOs.

2010-11 budget provisional language restricts expenditure of the $5 million GF provided for CVSOs and OWH. The language permits the DOF to authorize expenditure of the funds subject to 30-day prior notification to the Joint Legislative Budget Committee (JLBC) and the fiscal committees of the Legislature. The DOF notification is required to include a CDVA plan detailing: (1) the process for awarding the funds; (2) how CDVA will measure performance of funding recipients; (3) the related data collection instrument; and (4) efforts to coordinate funding recipients and other agencies working on OWH. While CDVA submitted a plan to JLBC on December 22, 2010, DOF has not provided notice of intent to authorize expenditure of the funds. Without such DOF authorization, the funds will not be spent by CDVA or CVSOs and instead will be GF savings for 2010-11.

Background. Established in 1946, CVSOs are local agencies that assist veterans in receiving the federal benefits for which they are eligible and act as the CDVA's network for claim initiation and development.

OWH began in February 2010 under the prior Administration. OWH is intended to assist veterans in receiving coordinated assistance including job placement, unemployment benefits, housing, healthcare, and federal, state, and local veterans' benefits and services. OWH was initially funded with a $20.0 million one-time federal Labor Department grant and a three-year $700,000 AmeriCorps grant. The $20.0 million grant expired as of December 31, 2010. The $5 million provided in the 2010-11 Budget was ongoing funding intended to sustain OWH.

Current law requires that the proceeds of the Veterans Service Office Fund, which is comprised of revenues from the sale of special license plates, be used to support CVSOs.

Staff Comment. The Administration's 2011-12 request is to eliminate the $2.6 million base funding for CVSOs and the $5 million OWH augmentation first provided in 2010-11.

Were the Legislature to adopt the Governor's 2011-12 proposal to eliminate the $2.6 million provided to CVSOs, CVSO funding would be reduced by 15 to 17 percent in the aggregate. CDVA also estimates that approximately half of the CVSOs currently operating would cease their operations entirely. Given that the $2.6 million represents only 15 to 17 percent of CVSO funding, it is not clear that the state's investment is sufficient to generate a real return in terms of what workload CVSO's focus on day-to-day.

Staff notes that it could also be argued that eliminating state GF support for CVSOs is consistent with the Administration's larger plan to realign government functions by restoring to local government the authority to make decisions that are best made closer to the people, not in Sacramento. However, unlike other functions proposed for realignment in 2010-11 for which the Administration provides dedicated and ongoing revenues, no funding is proposed for CVSOs or OWH. The Administration's own budget documents state that CVSOs act as the CDVA's network for claim initiation and development and assist veterans in receiving the federal benefits for which they are eligible. It is also worth noting that $838,000 of the $2.6 million in base funding serves as a match for Medi-Cal for the CVSO's Medi-Cal Cost Avoidance activities to move veterans off of Medi-Cal and onto federal veterans' benefits thereby saving the state GF.

Staff Recommendation: Hold open.

Vote:

Senate Budget and Fiscal Review—Mark Leno, Chair

SUBCOMMITTEE NO. 4 Agenda

Senator Michael J. Rubio, Chair
Senator Noreen Evans
Senator Doug LaMalfa

Monday, February 7, 2011
2:30 p.m. or Upon Adjournment of Session
Room 112

Consultant: Kris Kuzmich

PART A

OUTCOMES

Item Number and Title

0502	California Technology Agency
8855	Bureau of State Audits
8955	California Department of Veterans Affairs

(See Table of Contents on page 2 for a More Specific Listing of Issues)

Pursuant to the Americans with Disabilities Act, individuals who, because of a disability, need special assistance to attend or participate in a Senate Committee hearing, or in connection with other Senate services, may request assistance at the Senate Rules Committee, 1020 N Street, Suite 255 or by calling 916-324-9335. Requests should be made one week in advance whenever possible.

AGENDA – VOTE ONLY ITEMS

(Please see summary chart on Page 3)

AGENDA – DISCUSSION / VOTE ITEMS

Issues Proposed for Vote Only:

	Issue	2011-12 Amount	Fund Source	Staff Recommendation
	California Department of Veterans Affairs (8955)			
1	Yountville Veterans Home: Veterans' Cemetery Renovation	$2.4 million	Federal Funds	APPROVE
2	Yountville Veterans Home: Chilled Water Distribution System	$2.236 million	Lease Revenue Bond Funds	APPROVE
3	Yountville Veterans Home: Steam Distribution System Renovation	$3.387 million	Lease Revenue Bond Funds	APPROVE

Vote: Budget requests approved on a 2-0 vote; Senator Evans absent.

Issues Proposed for Vote Only – Issue Descriptions

CALIFORNIA DEPARTMENT OF VETERANS AFFAIRS (8955)

For overview and budget information regarding this department, please see page 12 of this agenda.

Issue 1 – Yountville Veterans Home: Veterans' Cemetery Renovation

Governor's Request. The Governor requests $2.4 million (federal funds) for the construction phase of the Yountville Veterans Home cemetery restoration project. General obligation bonds have previously been approved in the amount of $436,000 for the preliminary plans and working drawing phases of the project. The complete project costs total $2.847 million and will be fully reimbursed by the federal government once the grant is awarded.

Background. The cemetery at the Yountville Veterans Homes is the second oldest veterans' cemetery in the nation covering approximately 10.27 acres. The cemetery is reserved for veterans who reside at any CDVA veterans home. The condition of the cemetery over the past several decades has continued to deteriorate and is considered to be in a severe state of disrepair. More specifically, much of the cemetery infrastructure, including the sewage and water distribution systems, need to be repaired and/or replaced. The objectives within this restoration project will bring the cemetery into compliance with the National Cemetery Administration standards and enable the state to maintain the cemetery grounds according to those standards in future years.

Issue 2 – Yountville Veterans Home: Chilled Water Distribution System Renovation

Governor's Capital Outlay Request. The Governor requests $2.236 million (lease revenue bonds) to correct system deficiencies in the Chilled Water System at the Yountville Veterans Home. The additional chiller plant and replacement of cooling towers, pumps, and valves will ensure the Yountville Home has the required chiller capacity to maintain a proper temperature throughout the Home to protect the health and safety of the elderly and/or disabled veteran residents. The total estimated project cost is $6.398 million and will be funded by: (1) $497,000 – Veterans' Home Bond; (2) $2.236 million – Lease Revenue Bonds; and (3) $3.665 million – Federal Trust Fund.

Background. The chilled water system at the Yountville Home does not maintain the water at the proper temperature when the outside air temperature exceeds 96°F. As a result, patient areas exceed temperature limits mandated by the California Department of Health Services. Due to other system deficiencies (e.g., cooling towers, pumps, and valves), additional capacity solely on its own will not allow the cooling system to efficiently and effectively meet the increased demand on the chilled water cooling system. The project will renovate the chilled water system by adding chiller capacity and replacing cooling towers, chilled water pumps, condenser water pumps, automatic flow control valves, automatic water isolation valves, and bypass circuit and automatic valves. A new

400 ton chilled water system will be installed adjacent to Holderman Hospital along with a 400 kW generator to provide emergency/back-up power.

Issue 3 – Yountville Veterans Home: Steam Distribution System Renovation

Governor's Capital Outlay Request. The Governor requests $3.387 million (lease revenue bonds) to renovate the deteriorating underground steam distribution system at the Yountville Veterans Home. The project includes replacement of underground lines and valves and removal and replacement of badly deteriorated asbestos insulation that is a safety hazard. As part of landscaping an area disrupted by the steam lime replacement project, 10 ADA-accessible parking spaces will be provided to an underserved part of the Home. The total estimated project cost is $7.482 million and will be funded by: (1) $3.387 – Lease Revenue Bonds; and (2) $4.095 million – Federal Trust Fund.

Background. Steam provides heating and domestic hot water to all 120 buildings that serve the elderly and disabled veterans who reside at the Yountville Home. Steam is also instrumental in preparation of food for all residents. Furthermore, steam is used to keep the food warm to be served in the seven dining rooms used by residents or by bedside services. Last, steam is used by the heat exchanger to provide cooling for the buildings and residential areas. The steam lines are currently insulated using asbestos containing material and are badly deteriorated. As a result, loose asbestos containing material is present in several manhole accesses throughout the facility.

This project will also add 10 ADA-accessible parking spots to the Section A residence. This residence currently houses 90 members, but only has 12 parking spaces. Because the steam line renovation will disturb the landscaping adjacent to the residence, it is cost effective to fold the additional parking spaces into this project. A stand-alone parking project of this size would be unable to garner federal participation.

Renovation of the steam distribution system will ensure a safer and more energy efficient operation and the uninterrupted availability of steam for the Yountville Home's critical daily operations.

0502 CALIFORNIA TECHNOLOGY AGENCY

Department Overview. The California Technology Agency (CaTA) establishes and enforces statewide information technology (IT) strategic plans, policies, standards, and enterprise architecture, and oversees IT projects and public safety emergency communications systems for all state departments. Effective January 2, 2011, Chapter 404, Statutes of 2010 (AB 2408), renamed the Office of the State Chief Information Officer the "California Technology Agency" and codified the statewide IT consolidation originally implemented by the Governor's Reorganization Plan No. 1 in 2009.

The Officer of Technology Services (OTech) within CaTA, provides the IT processing platforms for over 500 customers, including the Executive Branch and public entities. OTech is accountable to its customers for providing secure services that are responsive to their needs and represent best value to the state. The OTech is a fee-for-service organization and operates as a 100 percent reimbursable department. OTech's Service Level Agreements (SLAs) with its customers include a 99.9 percent service availability goal for IT services. The OTech must continue to provide sufficient processing capacity to deliver the performance and service agreed to in the SLAs.

Budget Overview. The January Governor's Budget provides 1,364.2 authorized positions and $486.2 million ($3.7 million GF). The increased funding primarily reflects additional expenditure authority associated with increased computer system utilization at the state level, including mainframe processing, data storage, and server capacity.

Issues Proposed for Discussion / Vote

Issue 1 – Mainframe Processing Capacity, Database Hosting, Data Storage, and Email Hosting

Governor's Budget Request. The Governor requests total increased expenditure authority of $29.7 million (Technology Services Revolving Fund) and 23 positions. The increased expenditure authority is associated with increased computer system utilization at the state level, including mainframe processing, data storage, and server capacity, as illustrated in the below chart. Note, each item is described in detail beginning on the next page. The fund source for all items is the Technology Services Revolving Fund.

	2010-11 Funding Level	Description	Positions
Mainframe CPU Processing	$5.499 million	1.616 million of Instructions Per Second (MIP)	
Midrange Server	$8.186 million ($2.044 ongoing)	95 addition UNIX server instances and 412 additional Windows server instances	20.0
Data Storage Capacity	$5.366 million	Hardware, software, and connectivity components	
CA.mail and California Email Services	$10.639 million	Implement vendor hosted California Email Services	3.0

Mainframe CPU Processing

The CaTA, on behalf of the OTech, requests increased expenditure authority of $5.499 million (Technology Services Revolving Fund) in 2011-12 for the purchase of mainframe processing capacity [1.616 million of Instructions Per Second (MIPS)] to accommodate existing and projected increases in workload resulting from customer program growth and program changes. Costs included in this request are based on current pricing for this type of upgrade, plus the costs of supporting the components. Of OTech's current total of 500 customers, approximately 250 are mainframe processing customers. New state anti-fraud initiatives, federal reporting requirements, and natural population and caseload growth have driven a projected 14 percent increase in mainframe transactions for 2011-12. OTech's capacity must increase to provide sufficient resources for customer workloads because OTech acquires processing capacity only as needed for current workloads; i.e., the projected growth cannot be absorbed into the existing computing infrastructure.

Midrange Server

The CaTA, on behalf of OTech, requests increased expenditure authority of $8.186 million (Technology Services Revolving Fund) in 2011-12 to: (1) purchase 95 additional UNIX server instances and 412 additional Windows server instances for growth; (2) replace 25 UNIX servers and 50 replacement Windows server instances; and (3) add 20.0 permanent staff for the support of server instances, databases, and web services. Of the total funding requested, one-time costs are $6.142 million for the UNIX and Windows server instances and software cost and ongoing costs are $2.044 million for the 20 additional positions. OTech's processing capacity must continue to increase to meet the ever growing IT demands of its 500 customers. Governmental programs increase their reliance on technology to meet growing program workload with greater efficiency. This saves the taxpayer funds overall, but results in a continual increase in: (1) the number of installed servers at OTech; (2) related refresh/replacement of servers; and (3) tasks needed to provide support services for this growth.

Data Storage Capacity

The CaTA, on behalf of the OTech, requests increased expenditure authority of $5.366 million (Technology Services Revolving Fund) in 2011-12 for hardware, software, and connectivity components to ensure adequate data storage support to meet needs of customer driven workloads. Without capacity upgrades and growth, OTech will be unable to support the growth of customer programs, the systems will reach capacity, and customers will be unable to add new data.

CA.mail and California Email Services

The CaTA, on behalf of the OTech, requests increased expenditure authority of $10.639 million (Technology Services Revolving Fund) in 2011-12 and three positions to implement the vendor hosted California Email Services (CES). The increased expenditure reflects the requirement in Executive Order S-03-10, and statutorily in Chapter 404, that all executive branch agencies are required to migrate to either the OTech operated CA.mail or the third party hosted CES by June 2011. The migration will improve security and standardization of IT across State government.

CaTA Prior Year Project Adjustments

The Governor requests prior year baseline adjustments for the CaTA's expenditure authority to align previously approved budget actions with the ongoing costs of the related projects. The adjustments result in a net reduction of $10.2 million (Technology Services Revolving Fund) in 2010-11 and $10.0 million (Technology Services Revolving Fund) in 2011-12. The purpose of these adjustments is to align the OTech budget with actual expenditures in order to maintain a connection between spending authority level of OTech and the actual expenditures required to support the needs of its customers.

Staff Comment. These requests are consistent with the consolidation of IT within the CaTA, which the Legislature approved in 2009 with the adoption of the Governor's Reorganization Plan No. 1. The CaTA, and OTech more specifically, must continue to provide sufficient computing capacity to deliver performance and service to its customers. These requests are integral to OTech meeting that charge and providing its customers with the agreed upon service levels.

Staff Recommendation: Approve the budget requests.

Vote: Budget requests approved on a 2-0 vote; Senator Evans absent.

Issue 2 – Independent Project Oversight

Governor's Budget Request. The Governor requests $966,000 (Technology Services Revolving Fund) and nine permanent positions for Independent Information Technology Project Oversight (IPO) in 2011-12 and ongoing to meet workload increases and mandated responsibilities of Chapters 183 and 404, Statutes of 2007 (SB 90) and Statutes of 2010 (AB 2408), respectively, and to ensure consistent project implementation of the state's IT projects.

Background. The increased expenditure authority in this request is for a staffing expansion that the CaTA considers a critical priority due to legislative mandates, increased public visibility, and the need to ensure consistent project implementation of the state's IT projects. These positions would provide independent project management services to customer departments. The costs associated with the IT project management will be funded by the agency or department administering the project. The CaTA would be reimbursed 100 percent by the department or agency requesting the services. Once the CaTA has created a professional state governmental entity, comprised of state staff, to manage and direct IT policy, standards, and projects, the state's current reliance on high paid contractors will be diminished. The state currently spends approximately $17.2 million annually on contracted IT project oversight and management.

Staff Comment. The proposed positions represent the beginning of the implementation of CaTA's expanded role as outlined in Chapter 404. Staff concurs that having IPO conducted in-house (as opposed to contracted out) will save the state as the state will no longer rely on highly paid contractors and will instead develop a cadre of IT professionals within state service. However, in considering this request, the Subcommittee may wish to defer action until later in the Spring so that all factors and the CaTA's resources can be considered at one time.

Staff Recommendation: Deny the budget request without prejudice and consider as part of the Spring 2011 budget process.

Vote: Budget request denied without prejudice on a 2-0 vote; Senator Evans absent.

8855 BUREAU OF STATE AUDITS

Department Overview. The California State Auditor (Auditor) promotes the effective and efficient administration and management of public funds and programs by providing citizens and government nonpartisan, accurate, and objective assessments of state and local governments' financial and operational activities. As the independent auditor, the Auditor is the only state entity that the law grants full access to all records of state and local agencies, special districts, school districts, and any publicly created entity.

The Auditor conducts: (1) performance, financial, or compliance audits that are either mandated by statute or requested by the Legislature through the Joint Legislative Audit Committee (JLAC); (2) California's Single Audit, a combination of the independent audit of the State's basic financial statements and the independent audit of numerous federal programs administered by the State, which is required as a condition for the state to receive billions in federal funds each year; and (3) evaluations of those issues and entities identified as being high risk. Statutorily-required audits are the first priority for the Auditor, followed by those approved by the JLAC, and then those audits conducted under the Auditor's high-risk authority.

Finally, under the California Whistleblower Protection Act, the Auditor has broad authority to perform independent investigations into complaints that state employees or agencies have engaged in improper conduct. Additionally, the Auditor administers California's Whistleblower Hotline that enables the public to report improper acts committed by state agencies, departments, or employees.

Budget Overview. The January Governor's Budget provides $24.8 million ($14.0 million GF) and 181 positions. This is an increase of $8.2 million ($4.7 million GF) and 34 positions. Year-to-year, the Auditor's Budget shows only a net increase of $5.5 million, but this is due to a reduction in contract audit work and American Recovery and Reinvestment Act audit and oversight work.

Issue Proposed for Discussion / Vote:

Issue 1 – Budget Augmentation

Governor's Budget Request. The State Auditor requests an increase of $8.2 million ($4.7 million GF) and 34 positions in 2011-12 to fund a two-year plan to better assist the Legislature in its oversight of government operations, including conducting additional audits, completing more high risk analyses, and better integrating the audit process with the work of legislative budget and policy committees.

Background. The State Auditor requests the increased funding as part of a two-year plan to better assist the Legislature in its oversight of government operations. Currently, the Auditor has 147 staff. In Year 1 of this plan, the Auditor proposes to increase staffing by 34 positions, to a total of 181 positions. In Year 2, an additional 37 staff would be added, bringing staffing to a total of 218 positions. The following chart illustrates this two-year staffing plan:

Staffing Categories	Current Level 2010-11	Year One 2011-12	Year Two 2012-13	Total
Audit	93	28	26	147
Investigative	9	3	5	17
Information Technology	6	2	2	10
Executive Office	6	1	2	9
Legal	4	0	2	6
Administration/Support	29	0	0	29*

**The support staff number may grow slightly during the two-year plan; if so, the number of audit positions would be decreased by a like amount.*

In Year 1, the Auditor reports that it will utilize $3.5 million of the requested funding to contract with outside experts to conduct the federal compliance audit work, thereby allowing the Auditor to utilize the remaining $4.5 million to recruit, hire, and train the 34 new in-house staff to conduct the additional mandated, discretionary, and high-risk audit work as well as investigations. These 34 staff will also respond to increases in other activities, such as inquiries and requests from legislative staff, legal assistance, and public record requests, due to the additional audits being completed.

In Year 2, the Auditor reports that it should have a sufficient number of trained audit and investigative staff to conduct the increase in audit work and provide the additional integration with legislative oversight. Consequently, in Year 2, the Auditor plans to substantially reduce or eliminate the contracted federal compliance work to hire the additional 37 staff.

At the end of the two-year plan, which will result in the addition of 54 new audit staff, the Auditor reports that audit production will increase from the 2010-11 average of 30 per year, to 50-55 per year, including discretionary and mandated audits, as well as more work under the high-risk authority. The additional audit staff will also reduce the time it currently takes to complete an audit, and will also reduce staff burnout and a high turnover rate. The Auditor reports that the addition of eight investigative staff over the two years will result in self-initiated statewide investigations increasing from the 2010-11 average of one per year to four to eight per year.

Chapter 160, Statutes of 2010 (AB 1749), extends the protections under the California Whistleblower Protection Act to employees of the Judicial Branch. The Auditor indicates that the expansion of its Investigative Unit under the two-year plan is due in part to the expected increase in Whistleblower activity resulting from this change in law.

The Auditor indicates that the additional audit and investigative results from the two-year plan will produce more monetary benefits for the state, and offers the following recent examples of savings from audit and investigative work: (1) $194 million in unallowable costs, plus $53 million in cost avoidance over seven years (State Mandates Audits, 2003 and 2009); (2) $3.3 million revenue increase (Citation Penalty Accounts, 2010-108); (3) $4.8 million in cost avoidance (Medi-Cal TARS, 2009-112); and (4) $12 million cost recovery (CalWorks, 2009-101)

Staff Recommendation: Approve the budget request.

Vote: Budget request held open.

8955 CALIFORNIA DEPARTMENT OF VETERANS AFFAIRS

Department Overview. The California Department of Veterans Affairs (CDVA) promotes and delivers benefits to California veterans and their families. More specifically, the CDVA provides: (1) California veterans and their families with aid and assistance in presenting their claims for veterans' benefits under the laws of the United States; (2) California veterans with beneficial opportunities through direct low-cost loans to acquire farms and homes; and (3) the state's aged and disabled veterans with rehabilitative, residential, and medical care and services in a home-like environment at the Veterans Homes of California (VHCs). The CDVA operates VHCs in Yountville (Napa County), Barstow (San Bernardino County), Chula Vista (San Diego County), and Greater Los Angeles Ventura County (with homes in West Los Angeles, Ventura, and Lancaster).

Budget Overview. The January Governor's Budget proposes to continue to ramp-up admissions at the VHCs in West Los Angeles, Lancaster, and Ventura. The Governor also proposes to provide continued resources and staffing related to the construction and activation of two new VHCs, in Redding and Fresno, both of which are scheduled to begin admissions in early calendar year 2012. The January Governor's Budget provides CDVA with 2,396.5 authorized positions and $399.3 million ($253.4 million GF).

The construction cost of the VHCs was/is funded with $50 million in general obligation bonds available through Proposition 16 (2000), an estimated $212 million in lease-revenue bonds [most recently amended by Chapter 824, Statutes of 2004 (AB 1077)], and federal funds.

Issues Proposed for Discussion / Vote:

Issue 1 – Program 30, Veterans Homes of California

Governor's Request. The Governor requests a net GF increase of $39.8 million in 2011-12 for all of the VHCs, including: (1) an augmentation of $32.1 million for full-year and one-time adjustments to phase-in staffing and residents in the existing and new VHCs in Greater Los Angeles Ventura County (GLAVC), Redding, and Fresno; (2) $4.7 million for furlough and personal leave program reductions which are only reflected in the 2010-11 fiscal year budget; and (3) $9.3 million in increased lease-revenue bond payments for VHC-GLAVC. The expenditures are offset by an increase of $5.8 million in GF revenue.

2010-11 Budget. The 2010-11 budget provided the following for the VHCs: (1) VHC-GLAVC, 101.3 positions and $7.5 million GF to continue construction, activate business, and begin admitting veterans; and (2) VHC-Redding and VHC-Fresno, respectively, 9.3 positions and $908,000 GF, and 8.5 positions and $908,000 GF, for Construction Completion and Pre-Activation Phase II activities.

Background. The CDVA provides residential and medical care services to honorably discharged California veterans who served on active duty and are over the age of 62 or disabled. The VHCs are long-term residential care facilities that provide California's qualified aged or disabled veterans with rehabilitative, residential, medical, and support services in a home-like environment. Once an eligible veteran selects a VHC as his or her long-term care option, and is approved for admission, the veteran becomes a fee paying resident of the VHC. Home residents are veterans of military service ranging from World War II, Korea, Vietnam, Gulf War I, and Operation Enduring Freedom and Operation Iraqi Freedom. Spouses of veterans may also be eligible for VHC membership. The VHCs provide a long-term continuum of care, from domiciliary care at one end of the spectrum, which is similar to independent living accommodations, to skilled nursing care at the other end of the spectrum, which provides continuous skilled nursing or rehabilitation services. The chart below illustrates the six VHCs that are currently operating, including their licensed bed capacity and levels of care provided:

Veterans Homes of California

	Yountville	**Barstow**	**Chula Vista**	**West Los Angeles**	**Lancaster**	**Ventura**
Year Established	1884	1996	2000	November 2010	February 2010	January 2010
Licensed Beds*	1,207	344	400	84	60	60
Domiciliary Care	Yes	Yes	Yes	No	No	No
Residential Care Facility for the Elderly	Yes	No****	Yes	Yes	Yes	Yes
Intermediate Care Facility	Yes	Yes	No	No	No	No
Skilled Nursing Care	Yes	Yes	Yes	Yes***	No**	No**
Memory Care	Yes	Yes	Yes	Yes	No	No

**Includes suspended beds.*
***Residents needing SNF care at VHC-Ventura or VHC-Lancaster will transfer to VHC-West Los Angeles.*
****To be added in 2011-12.*
*****Barstow is not currently licensed or budgeted for the Residential Care Facility for the Elderly level of care.*

The VHC-Redding and VHC-Fresno facilities are scheduled to open in early calendar year 2012. Both of these homes will provide the following levels of care: Residential Care Facility for the Elderly and Skilled Nursing Care, including Memory Care services within each level of care.

Staff Comment. Staff agrees with the need to adequately and appropriately staff the VHC-GLAVC facilities, as well as VHC-Redding and VHC-Fresno. CDVA indicates that the hiring and occupancy timeframes have been updated to reflect admission schedules and level-of-care offerings at these homes. Further, CDVA indicates that it utilizes a “point-in-time” hiring approach, where staff is added as resident admissions increase. However, it is worth noting that in past years when this Subcommittee considered similar VHC requests, and after the May Revision when caseloads are updated, some salary savings have been found because not all of the positions contained in the requests would be hired per the updated schedules.

Staff also notes that some questions have arisen about veteran demand at the GLAVC facilities. More specifically, both VHC-Lancaster and VHC-Ventura have been open since January and February 2010, respectively. Both homes were scheduled to admit eight residents per month for the first three months and then five residents each month thereafter until their budgeted capacity of 54 was reached in August and September 2010, respectively. As of January 17, 2011, VHC-Lancaster had 22 residents; VHC-Ventura had 39 residents. VHC-West Los Angeles opened in October 2010. It is scheduled to admit eight residents per month for the first three months and then five residents each month thereafter until it reaches its budgeted capacity of 39 as of July 2011. As of January 17, 2011, VHC-West Los Angeles had 21 residents.

The CDVA indicates that both VHC-West Los Angeles and VHC-Ventura are on track to reach their census goal of 39 and 54 respectively by the end of the 2010-11 fiscal year; for VHC-Ventura, this is ten months longer than the original schedule. In the case of VHC-Lancaster, CDVA indicates that the home may not reach its goal. The CDVA indicates that there is presently a lack of demand and applications for VHC-Lancaster; the CDVA indicates that it is engaged in a focused marketing and outreach campaign to reverse the situation. Regardless, given the current resident census at the GLAVC facilities, staff notes that there will likely be salary savings in the 2010-11 budget due to the pace of admissions and admission levels at both VHC-Ventura and VHC-Lancaster. Staff does not recommend making any current year adjustments, as five months remain in the 2010-11 year and any savings will revert to the GF automatically. However, this situation presents a challenge for the Subcommittee in its consideration of the 2011-12 request for VHC-GLAVC, as well as for VHC-Redding and VHC-Fresno.

Given the expedited timeframe for adoption of the 2010-11 budget, it will not be possible to know now what budget adjustments might need to be made to the VHC caseloads and budget post the May Revision, including if the situation at VHC-Lancaster does not reverse itself. However, it is known that some portion of the resources contained in this request will be needed at the GLAVC, Redding, and Fresno VHCs. Therefore, while staff recommends approval of this request, staff also recommends the Subcommittee clearly state its intent to reopen the VHC budget in Spring 2011 when caseloads are better known to make necessary adjustments to the 2011-12 budget.

Staff Recommendation: Approve the budget request but state intent to reopen the Veterans Home of California budget in Spring 2011 when caseloads are known and to make any necessary adjustments to the 2011-12 budget.

Vote: Budget request approved on a 2-0 vote; Senator Evans absent. Subcommittee stated its intent to reopen the VHC budget in Spring 2011.

Issue 2 – County Veterans Service Offices / Operation Welcome Home

Governor's Budget Request. The Governor requests to eliminate $9.9 million GF ($7.6 million local assistance and $2.3 million state operations) support for County Veterans Service Offices (CVSOs) and Operation Welcome Home (OWH) in 2011-12.

2010-11 Budget. The 2010-11 Budget provided baseline funding of $2.6 million GF and $544,000 (Veterans Service Office Fund - VSOF) to counties for CVSOs. The $2.6 million GF figure has been static since 2004. In addition, the 2010-11 Budget provided new funding to implement and sustain OWH as follows: (1) $5 million GF in ongoing operations funding for CVSOs, Veterans Service Organizations, and Non-Profit Organizations that provide services to veterans; and (2) a one-time VSOF augmentation of $768,000 to be spent over three years to implement the Subvention Administrative Information System, a common veteran case management application in CVSOs.

2010-11 budget provisional language restricts expenditure of the $5 million GF provided for CVSOs and OWH. The language permits the DOF to authorize expenditure of the funds subject to 30-day prior notification to the Joint Legislative Budget Committee (JLBC) and the fiscal committees of the Legislature. The DOF notification is required to include a CDVA plan detailing: (1) the process for awarding the funds; (2) how CDVA will measure performance of funding recipients; (3) the related data collection instrument; and (4) efforts to coordinate funding recipients and other agencies working on OWH. While CDVA submitted a plan to JLBC on December 22, 2010, DOF has not provided notice of intent to authorize expenditure of the funds. Without such DOF authorization, the funds will not be spent by CDVA or CVSOs and instead will be GF savings for 2010-11.

Background. Established in 1946, CVSOs are local agencies that assist veterans in receiving the federal benefits for which they are eligible and act as the CDVA's network for claim initiation and development.

OWH began in February 2010 under the prior Administration. OWH is intended to assist veterans in receiving coordinated assistance including job placement, unemployment benefits, housing, healthcare, and federal, state, and local veterans' benefits and services. OWH was initially funded with a $20.0 million one-time federal Labor Department grant and a three-year $700,000 AmeriCorps grant. The $20.0 million grant expired as of December 31, 2010. The $5 million provided in the 2010-11 Budget was ongoing funding intended to sustain OWH.

Current law requires that the proceeds of the Veterans Service Office Fund, which is comprised of revenues from the sale of special license plates, be used to support CVSOs.

Staff Comment. The Administration's 2011-12 request is to eliminate the $2.6 million base funding for CVSOs and the $5 million OWH augmentation first provided in 2010-11.

Were the Legislature to adopt the Governor's 2011-12 proposal to eliminate the $2.6 million provided to CVSOs, CVSO funding would be reduced by 15 to 17 percent in the aggregate. CDVA also estimates that approximately half of the CVSOs currently operating would cease their operations entirely. Given that the $2.6 million represents only 15 to 17 percent of CVSO funding, it is not clear that the state's investment is sufficient to generate a real return in terms of what workload CVSO's focus on day-to-day.

Staff notes that it could also be argued that eliminating state GF support for CVSOs is consistent with the Administration's larger plan to realign government functions by restoring to local government the authority to make decisions that are best made closer to the people, not in Sacramento. However, unlike other functions proposed for realignment in 2010-11 for which the Administration provides dedicated and ongoing revenues, no funding is proposed for CVSOs or OWH. The Administration's own budget documents state that CVSOs act as the CDVA's network for claim initiation and development and assist veterans in receiving the federal benefits for which they are eligible. It is also worth noting that $838,000 of the $2.6 million in base funding serves as a match for Medi-Cal for the CVSO's Medi-Cal Cost Avoidance activities to move veterans off of Medi-Cal and onto federal veterans' benefits thereby saving the state GF.

Staff Recommendation: Hold open.

Vote: Rejected Governor's proposal to eliminate funding for CVSOs and Operation Welcome Home in 2011-12 and adopted revised BBL to require release of Operation Welcome Home funds on a 2-0 vote; Senator Evans absent.

Senate Budget and Fiscal Review—Mark Leno, Chair

SUBCOMMITTEE NO. 4 Agenda

Senator Michael J. Rubio, Chair
Senator Noreen Evans
Senator Doug La Malfa

Monday, February 7, 2011
2:30 p.m. or Upon Adjournment of Session
Room 112

Consultant: Seija Virtanen

PART B

<u>Item Number and Title</u>

1100	California Science Center
1110	Department of Consumer Affairs, Boards
1111	Department of Consumer Affairs, Bureaus
2150	Department of Financial Institutions
2400	Department of Managed Health Care

(See Table of Contents on page 2 for a More Specific Listing of Issues)

Pursuant to the Americans with Disabilities Act, individuals who, because of a disability, need special assistance to attend or participate in a Senate Committee hearing, or in connection with other Senate services, may request assistance at the Senate Rules Committee, 1020 N Street, Suite 255 or by calling 916-324-9335. Requests should be made one week in advance whenever possible.

AGENDA – VOTE ONLY ITEMS

(Please see summary chart on Page 3)

AGENDA – DISCUSSION / VOTE ITEMS

Issues Proposed for Vote Only:

	Issue	2011-12 Amount	Fund Source	Staff Recommendation
	Department of Consumer Affairs, Boards (1110/1111)			
1	Board of Accountancy: Enforcement Division Staffing Augmentation	$0 (position authority only)	Special Funds	APPROVE
2	Physician Assistant Committee: Increase Reimbursement Authority	$25,000	Special Funds	APPROVE
3	State Board of Optometry: Staff Services Manager I Position	$0 (position authority only)	Special Funds	APPROVE
4	Various Bureaus: Baseline Funding Reduction	-$3.2 million combined	Various Special Funds	APPROVE
	Department of Managed Health Care (2400)			
5	Health Care Reform	$1.4 million	Special Funds	APPROVE

Vote:

Issues Proposed for Vote Only – Issue Descriptions

DEPARTMENT OF CONSUMER AFFAIRS, BOARDS (1110)
DEPARTMENT OF CONSUMER AFFAIRS, BUREAUS (1111)

For overview and budget information regarding this department, please see page 10 of this agenda.

Issue 1 – Board of Accountancy: Enforcement Division Staffing Augmentation

Board of Accountancy. Created by statute in 1901, the California Board of Accountancy's legal mandate is to regulate the accounting profession for the public interest. To accomplish this, the Board qualifies California candidates for the National Uniform Certified Public Accountant (CPA) Examination; certifies, licenses, and renews licenses of individual CPAs and Public Accountants (PA); and registers CPA and PA partnerships and corporations; receives and investigates complaints; and takes enforcement actions against licensees for violation of Board statutes and regulations.

The Board of Accountancy currently regulates over 77,000 licensees, the largest group of licensed accounting professionals in the nation, including individuals, partnerships, and corporations.

The 2010-11 Budget for the Board of Accountancy is $12.21 million and 82.5 positions. The proposed 2011-12 Budget for the Board of Accountancy is $11.45 million and 85.8 positions. The Board of Accountancy's funding comes from fees paid by the licensees deposited into the Accountancy Fund.

Governor's Budget Request. The Governor requests position authority only for 2.5 Associate Governmental Program Analysts. The cost of these positions is $205,000 annually and will be redirected from excess funding authority in the Accountancy Fund.

Background. The Board of Accountancy's Enforcement Program currently has 17 positions. With a licensee population of 77,000, this equates to over 4,500 licensees per position. The Enforcement Program is responsible for investigations of complaints, probation monitoring, investigation of unlicensed activity, and verification of continuing education. In 2009-10 there were 682 complaints and an additional 67 cases of unlicensed activity. The Enforcement Program's average time for dealing with complaints is 249 days, but 46 cases have currently been open for more than a year. The new requested positions are intended to bring the timeframe for closing all cases down under 12 months.

Issue 2 – Physician Assistant Committee: Increase Reimbursement Authority

Physician Assistant Committee. The mission of the Physician Assistant Committee (PAC) of the Medical Board of California is to protect and serve consumers through licensing, education, and objective enforcement of the Physician Assistant laws and regulations. The PAC licenses and regulates physician assistants; enforces laws and regulations relating to physician assistant practice; encourages utilization of physician assistants in medically underserved areas; seeks ways and means to rehabilitate drug and alcohol impaired physician assistants; and encourages development of new physician assistant training programs and expansion of existing programs.

Governor's Budget Request. The Governor requests $25,000 in increased reimbursement authority for the PAC. The increased reimbursement authority would be used towards enforcement expenses that include investigation, attorney general, and probation monitor costs as intended.

Background. The reimbursements come primarily from applicant fingerprint fees and cost recovery ordered through disciplinary actions. Also, in 2007, the PAC began requiring licensees placed on probation to pay their probation monitoring costs. The reimbursement funds are placed in the Physician Assistant Fund, and cannot be spent unless there is reimbursement authority provided in the Budget Act.

During the last four years, PAC has collected between $10,000 and $46,000 more in reimbursements than it had authority to spend. If reimbursement authority is provided, but there are no funds in the account, the PAC would not be able to move expenditures forward.

In previous years, the PAC was forced to stop program activities during the last quarter of the fiscal year because its enforcement budget had been expended and the extra reimbursements from cost recovery and probation monitoring could not be used to offset enforcement costs.

Issue 3 – State Board of Optometry: Staff Services Manager I Position

State Board of Optometry. The California Legislature created the Board in 1913 to safeguard the public's health, safety, and welfare through regulation of the practice of optometry. Business and Professions Code section 3010.1 mandates the Board's highest priority as protection of the public. The State Board of Optometry is mandated to protect the public from the unauthorized and unqualified practice of optometry and from unprofessional conduct by persons licensed to practice optometry through its licensing, regulatory, and disciplinary functions.

Governor's Budget Request. The Governor requests position authority only for one Staff Services Manager I (SSMI) to serve as the Enforcement Manager. The position will cost $93,000 annually and will be funded by a redirection from Operating Expenses and Equipment from the State Optometry Fund.

Background. Currently, there are approximately 7,000 active optometric licensees in California and the state gains approximately 200 new licensees each year from new graduates and out-of state doctors seeking licensure in California. The increase in the licensee population over the years has led to a workload increase in administrative, licensing, and enforcement-related activities for Board staff, as well as an increase in the number of staff.

Supervising the increased workload has fallen on the Executive Officer (EO), which has resulted in extensive overtime and failing to meet various deadlines related to executive-level and supervisory tasks and responsibilities, e.g., completing Board minutes, probationary reports and individual development plans (IDPs), preparing progressive disciplinary counseling memos, drafting legislative proposals, and updating the Board's Strategic Plan. An SSM I would be able to assist the EO with the day-to-day supervision of staff, and oversee personnel, budget, and business service functions relating to enforcement activities within the Board.

Specifically, the SSM I would:
1. Provide day-to-day supervision;
2. Plan, organize, and direct the day-to-day work of clerical/analytical staff;
3. Hire/train new employees;
4. Complete probationary reports, annual reviews and individual Development Plans (IDPs), progressive disciplinary counseling memo;
5. Review and approve time-off requests; etc.

Issue 4 – Various Bureaus: Baseline Funding Reduction

Governor's Budget Request. The Governor requests a decrease in baseline funding authority for 2011-12 and on-going for the following programs:
1. Board of Accountancy: -$1,000,000
2. Architects Board: -$100,000
3. Board of Occupational Therapy: -$34,000
4. Bureau of Automotive Repair: -$500,000

Background. These Boards and Bureaus have consistently had reversions at the end of the fiscal year. This baseline funding reduction is a technical adjustment to bring funding authority in line with actual spending.

DEPARTMENT OF MANAGED HEALTH CARE (2400)

For overview and budget information regarding this department, please see page 19 of this agenda.

Issue 5 – Health Care Reform

Governor's Budget Request. The Governor requests $1,776,000 for 13.0 two-year limited-term positions to address new workload resulting from the March 2010 federal Health Care Reform Legislation.

Background. On March 23, 2010, President Obama signed into law comprehensive health care reform, the Patient Protection and Affordable Care Act, which was subsequently modified by the Health Care and Education Reconciliation Act of 2010 (hereinafter referred to as "Health Care Reform"). Health Care Reform will fundamentally alter the availability and structure of health insurance, bring coverage for the first time to millions of Californians, and bring new coverage options for millions of enrollees who receive care through California Knox-Keene Licensed health plans and contracted medical groups.

In light of the recent enactment of Health Care Reform, DMHC must take immediate action to assess and address the impacts of the reform on its mission critical operations. In response to Health Care Reform, DMHC will have to develop state regulations, review health plan documentation to comply with the new law, and respond to consumer inquiries.

The Department of Managed Health Care (DMHC) has explained that the positions are requested on a two-year limited-term basis not because DMHC expects the workload to be temporary, but to monitor the activity that results from Health Care Reform to determine if the workload assumptions hold true. Over the course of the two years, once all impacts are considered and a better assessment of new Health Care Reform workload results, the department will submit a future Budget Change Proposal to address the new permanent workload generated by the Health Care Reform legislation.

1100 CALIFORNIA SCIENCE CENTER

Department Overview. The California Science Center is an educational, scientific, and technological center located in Exposition Park, a 160-acre tract in south Los Angeles. The Science Center has interactive exhibits on human inventions and innovations, the life processes of living things, and temporary exhibits. The California African American Museum (CAAM), also included in the park, provides exhibitions and programs on the history, art, and culture of African Americans. In addition, the Office of the Park Manager is responsible for maintenance of the park, public safety, and parking facilities.

Budget Overview. The January Governor's Budget provides 190 authorized positions and $28.1 million ($19.4 million GF). It should be noted that the California Science Center budget includes the California African American Museum, Exposition Park Management, and facilities bond repayments. The reduction to the Science Center's operations is $3.66 million General Fund.

Issues Proposed for Discussion / Vote

Issue 1 – Unallocated Budget Reduction

Governor's Budget Request. The Governor requests an unallocated reduction of $3,660,000 to the Science Center's budget. The Governor also requests budget bill language to allow the Science Center to collect an admissions fee.

Background. The unallocated reduction of $3.7 million is 20 percent of the amount of General Fund remaining after excluding amounts budgeted for lease-revenue payments ($4.8 million). The General Fund base used for the calculation is $18.3 million ($23.1 million total General Fund less the $4.8 million).

The Science Center's operations have been based on the value that everyone is allowed access, and thus no admission fee has been charged. The Science Center does charge for parking and the IMAX movie tickets.

Staff Comment. Approximately one-third of the Science Center's visitors are school groups, which would be unlikely to afford admissions fees for each student, due to the funding restrictions that local school districts are currently experiencing.

Staff thinks that there are some possibilities for the Science Center to raise revenue that does not compromise the Science Center's dedication to free admission. The Science Center already charges $8 for parking, and $25 for parking at special events. (The Science Center also charges for their IMAX movie tickets.) It may be possible to raise additional revenue through increasing the parking fee from $8 to $10. The increase in parking fees would also apply to events at Exposition Park, including football games and concerts. Based on past Science Center parking fee increase revenue collections, staff estimates that the Science Center can collect approximately $800,000 in new revenue from raising parking fees.

The Office of the Exposition Park Management has an executive director appointed by the Governor for the purpose of managing, scheduling, and administering all park related events, including oversight for the police and security services of the park.

All items impacting the state of the General Fund will be heard in full committee.

Staff Recommendation: Staff recommends this issue be kept open for full committee consideration.

Vote:

1110/1111 DEPARTMENT OF CONSUMER AFFAIRS

Departmental Overview and Mission. The Department of Consumer Affair's (DCA) Boards and Bureaus provide exams and licensing, enforcement, complaint mediation, education for consumers, and information on privacy concerns. DCA Boards and Bureaus establish minimal competency standards for more than 255 professions involving approximately 2.4 million professionals. There are currently 25 boards, a commission, three committees, and eight bureaus under the broad authority of the DCA.

Budget Overview. The Boards are budgeted under organizational code 1110, and the total proposed budget is $271.46 million (no General Fund) and 1,511.3 positions – an increase of $10.4 million and 35.6 positions over 2010-11.

The Bureaus are budgeted under organizational code 1111, and the total proposed budget is $231.34 million (no General Fund) and 1,386.6 positions – an increase of $14.2 million and 5.7 positions over 2010-11.

DCA Boards and Bureaus

(dollars in thousands)

		Positions		Expenditures	
		2010-11	2011-12	2010-11	2011-12
1	Board of Accountancy	82.5	85.8	$ 12,210	$ 11,452
2	Architects Board	30.1	30.1	$ 4,686	$ 4,760
3	Athletic Commission	13.7	13.7	$ 2,541	$ 2,613
4	Board of Behavioral Science	42.6	43.4	$ 8,090	$ 7,898
5	Barbering and Cosmetology	95.1	95.1	$ 17,303	$ 18,291
6	Contractors State Licensing	402.1	402.1	$ 57,514	$ 59,979
7	Dental Board	71.6	75.1	$ 12,652	$ 13,496
8	Dental Hygiene Committee	6.2	6.7	$ 1,242	$ 1,358
9	Guide Dogs for the Blind	1.5	1.5	$ 180	$ 187
10	Medical Board	265.5	276.7	$ 52,385	$ 55,843
11	Acupuncture Board	7.9	8.0	$ 2,548	$ 2,603
12	Physical Therapy Board	15.0	16.4	$ 2,910	$ 3,290
13	Physician Assistant Com.	4.7	4.8	$ 1,387	$ 1,418
14	Podiatric Medicine	4.6	4.6	$ 1,362	$ 1,381
15	Psychology	15.3	18.3	$ 3,879	$ 4,335
16	Respiratory Care Board	15.9	16.1	$ 3,035	$ 3,138
17	Speech-Language Pathology	8.1	8.2	$ 1,848	$ 1,615
18	Occupational Therapy	10.5	10.2	$ 1,417	$ 1,473
19	Board of Optometry	10.9	11.1	$ 1,654	$ 1,574
20	Naturopathic Medicine Com.	0.9	0.9	$ 130	$ 141
21	Board of Pharmacy	75.4	80.0	$ 13,021	$ 14,448
22	Engineers and Land Surveyors	65.6	65.6	$ 10,397	$ 10,774
23	Registered Nursing	128.0	135.6	$ 28,250	$ 29,242
24	Court Reporters Board	4.3	4.3	$ 1,096	$ 1,114
25	Veterinary Medical Board	12.4	12.0	$ 2,639	$ 2,757
26	Vocational Nursing	74.7	73.3	$ 14,743	$ 14,237
27	Arbitration Certification Prog.	7.6	7.6	$ 1,098	$ 1,107
28	Hearing Aid Dispensers	0.0	0.0	$ -	$ -
29	Security and Investigative	50.2	50.7	$ 11,363	$ 11,865
30	Private Postsecondary Ed.	55.8	55.8	$ 10,160	$ 9,368
31	Electronic and Appliance Repair, Home Furnishings, and Thermal Insulation	41.9	41.9	$ 7,108	$ 7,781
32	Automotive Repair	596.2	600.2	$ 182,192	$ 195,798
33	Telephone Medical Advise Services Bureau	0.9	0.9	$ 145	$ 148
34	Cemetery and Funeral	21.2	18.5	$ 4,006	$ 4,149
35	Professional Fiduciaries	1.6	1.6	$ 282	$ 308

Issue Proposed for Discussion / Vote:

Issue 1 – Board of Accountancy: Peer Review Program

Governor's Budget Request. The Governor requests position authority only for one position to address clerical workload in the Board of Accountancy's Peer Review Program.

Background. Business and Professions Code Section 5076 requires that accounting firms providing audit, review, or compilation (accounting and auditing) services undergo a systematic review (peer review) of their accounting and auditing practice to ensure the work performed conforms to professional standards. Business and Professions Code Section 5035.1 defines a firm to be a sole proprietorship, a partnership, or a corporation. Peer review will be required every three years for accounting firms providing accounting and auditing services. This law became operative January 1, 2010, with the first group of accounting firms required to report peer review-related information no later than July 1, 2011.

The Board of Accountancy anticipates that approximately 6,000 accounting firms will be required to undergo a peer review, about 2,000 annually. The Board of Accountancy will be phasing in the accounting firm population over a three-year period, with the first group of accounting firms required to report specific peer review information no later than July 1, 2011. The Board of Accountancy will mail the peer review reporting form to all licensees with a current license once every three years.

In order to handle the volume of peer review reporting forms, the Board of Accountancy has determined that an additional Office Technician will be required to process the forms and be responsible for sending notifications to newly-licensed CPAs, along with other clerical duties. The Board of Accountancy anticipates that approximately five percent, or approximately 100 accounting firms yearly, will receive a substandard peer review rating, which requires submission of the peer review report by accounting firms. The Board of Accountancy also anticipates that beginning fiscal year 2011-12, 30 accounting firms will be referred to the Enforcement Division annually for failing to undergo a peer review, with increased referrals the following years. The Office Technician will assist with referral intake and provide some clerical support to Enforcement staff.

Staff Comment. The Board of Accountancy anticipates that only about half of the peer review reporting would take place electronically. If more licensees choose to file their peer reviews electronically, or if fewer firms are referred to the Enforcement Division than projected, there may be less workload and the need for an additional Office Technician will be reduced.

Staff Recommendation. Approve as a two-year limited-term position.

Vote:

Issue 2 – Bureau of Automotive Repair: Consumer Assistance Program Funding Realignment and Augmentation

Bureau of Automotive Repair. The Bureau of Automotive Repair is responsible for regulating the automotive repair marketplace and administering the Smog Check Program. To carry out its mandate, the Bureau educates consumers, disciplines stations and technicians, seeks resolution to complaints, and licenses individuals and businesses. The Bureau also administers the nation's largest motor vehicle emissions reduction program.

Governor's Budget Request. The Governor requests $22.157 million and 12.3 positions from the Enhanced Fleet Modernization Subaccount in 2011-12 and ongoing. In addition, the Governor requests a reduction of $7.693 million and 8.0 positions from the High Polluter Repair or Removal Account.

Background. A key part of California's air quality emissions reduction strategy is to implement incentive-based air quality programs to encourage the early retirement and replacement of older vehicles with newer, cleaner ones. Older vehicles account for approximately 25 percent of the miles driven but contribute up to 75 percent of the emissions released. Reducing emissions from the older vehicles is a critical part of California's State Implementation Plan (SIP), which outlines the state's clean air strategy. The SIP is used by the federal government to determine the amount of federal transportation funds California will receive.

The Consumer Assistance Program (CAP) was started in 1997 and contains two parts: vehicle retirement and vehicle repair. Under the vehicle repair program, qualified low-income consumers can receive financial assistance of up to $500 to repair a vehicle that is unable to pass a biennial Smog Check inspection when it exceeds specified emission standards. To receive the repair assistance, eligible consumers must pay the initial $20 in repairs. Beginning in 2000, a directed vehicle repair program was started that allowed qualified consumers who owned a vehicle directed to a Test-Only or Gold Shield Smog Check station for an initial inspection to receive up to $500 in additional financial assistance toward emissions-related repairs after they paid the first $100 of repairs. Directed vehicles are identified by the Bureau of Automotive Repair.

Under the vehicle retirement program, until August 2010, consumers were paid $1,000 to retire a vehicle. These funds are not paid until after the vehicle is dismantled.

The passage of AB 787 (Hill, 2010) makes several additional changes to CAP. Under AB 787 the Bureau of Automotive Repair must offer all eligible low-income consumers an additional $500 to retire a vehicle through CAP. AB 787 also allows any vehicle that has been registered in California for two continuous years and has failed a lawfully required Smog Check inspection to be retired through CAP.

AB 787 also eliminates the provision of law authorizing owners of directed vehicles the ability to participate in the repair assistance option of CAP based solely on this designation and receive $500 toward emissions-related repairs.

Staff Comment. The expansion of the vehicle retirement program from a $1,000 payment to a $1,500 payment is anticipated to cost approximately $8 million annually in addition to the base costs of $14.1 million annually (for a total cost of about $22.1 million). The Bureau of Automotive Repair estimates that about 16,600 vehicles will be retired annually.

Savings result from the elimination of the directed vehicle part of the vehicle repair program. The Bureau of Automotive Repair data indicates that about 40 percent (or 18,682) of the vehicle repair eligible consumers participated in the directed vehicle program. The elimination of this program will lead to $7,603,600 in program savings and an additional $470,000 in administrative savings (total $8,073,600 in savings).

Staff Recommendation. Approve.

Vote:

Issue 3 – Various Boards and Bureaus: BreEZe

Governor's Budget Request. The Governor requests a realignment of existing BreEZe funding authority by $1.2 million in 2011-12. The funding is prior year funds that had not been spent. Previously, the Legislature had approved a schedule of funding with $2,283,000 for BreEZe in 2011-12, and this augmentation will bring the 2011-12 funding to $3,483,000.

The budget for BreEZe is as follows (years 2010-11 through 2014-15 total $20.3 million):

- 2010-11: $1,330,000 (redirected from existing resources)
- 2011-12: $3,483,000
- 2012-13: $3,600,000
- 2013-14: $6,219,000
- 2014-15 and ongoing: $6,125,000

Background. Licensing of businesses and professionals includes: processing applications and qualifying applicants, conducting exams/processing results, maintaining and analyzing licensing-related information, authorizing practice(s) and issuing licensing documents, renewing licenses, performing Family Support verification, creating a variety of management reports, and processing a multitude of other requests.

The BreEZe system will bring all of the DCA boards and bureaus into an integrated licensing and enforcement system. In addition, the licensees will be able to use the BreEZe system to renew their licenses and update their addresses on-line. Currently, the 40 boards and bureaus do not have integrated systems (so a person could hold a medical license and a pharmacy assistant license and it would not be known to the enforcement units). BreEZe will allow for secure cross-license checking for every DCA board and bureau, and provide the ability to interface with any other capable external systems used in the enforcement process, such as the Department of Justice, the Employment Development Department, or the Department of Public Health, once the appropriate agreements have been established authorizing the secured sharing of the data.

The DCA Office of Information Services has an Office of the Chief Information Officer approved Feasibility Study Report (FSR) proposal for the BreEZe project.

The DCA has structured the BreEZe cost proposal based on a “fee-per-transaction” payment model. Under this payment model, the solution vendor receives no payment prior to the State’s acceptance and use of the production system. Instead, the solution vendor will be compensated by assessing system clients with a transaction fee for specific master transactions. For the BreEZe system, the DCA is anticipating that the solution vendor will assess a $3 per transaction fee to boards and bureaus for each new application or $0.50 for each renewal processed through the new system.

The BreEZe Request for Proposals (RFP) was released in May 2010, and was met with concerns from bidders that the proposed payment model was overly burdensome and would limit the bidders’ ability to submit proposals to the state. DCA wants to change the RFP to provide a $1.2 million payment for the solution software following installation of the software on State equipment, and the State’s acceptance of the detailed solution design.

Staff Comment. Last year the Legislature requested a report on staffing workload needs once the BreEZe system is completed. The BreEZe system should be able to expedite the license renewal process and reduce the amount of paperwork that must be manually processed. The Legislature also requested a copy of the final vendor contract in order to ensure that costs remain reasonable.

Since the BreEZe system will automate much of the licensing renewal process it can potentially create great savings for the DCA boards and bureaus. Delays in contracting would also delay the actualization of these savings.

This augmentation does not increase the overall project costs, but rather takes current year unspent funds and offers them as a bidding incentive.

Staff Recommendation. Approve.

Vote:

Issue 4 – Board of Accountancy and Dental Board: Loan Repayment

Dental Board of California. The Dental Board of California establishes minimal standards of competency for those individuals seeking to practice as a dentist, registered dental hygienist, registered dental assistant, dental auxiliary in extended function, or dental hygienist in alternative practice. The Board enforces standards to protect California dental consumers from incompetent dental practitioners, and the utilization of dental auxiliaries contributes to providing quality dental services to Californians.

Effective January 1, 2009, the State Dental Assistant Committee (Committee) was created and assumed the duties of the Committee on Dental Auxiliaries with regard to dental assistants, pursuant to Chapter 31, Statutes of 2008 (SB 853).

Governor’s Budget Request. The Governor requests repayment of two loans from the General Fund to special funds: 1) $10 million repayment by the General Fund to the

Accountancy Fund, and 2) $2.5 million repayment by the General Fund to the State Dentistry Fund.

Background. During the 2010-11 fiscal year, the State loaned $10 million from the Accountancy Fund to the General Fund. This amount is set to be repaid in June 2012.

During the 2002-03 fiscal year, the State loaned $2.5 million from the State Dentistry Fund to the General Fund. This amount is set to be repaid in June 2012.

Staff Comment. The Accountancy Fund loan repayment can be delayed by one year without having an influence on the Board's programs.

$1.3 million of the loan from the State Dentistry Fund can be delayed by one year without having an influence on the Board's programs.

Staff Recommendation. Delay repayment of the Accountancy Fund $10 million loan until June 30, 2013. Include the following budget bill language:

Add Item 1110-404:
1110-404—Notwithstanding Provision 1 of Item 1110-011-0704, Budget Act of 2010 (Ch. 712, Stats. 2010), the $10,000,000 loan to the General Fund will be repaid in fiscal year 2012-13 upon order of the Director of Finance.

Delay repayment of $1.3 million of the State Dentistry Fund loan repayment until June 30, 2013. Include the following budget bill language:

Add Item 1110-405:
1110-405—Notwithstanding Provision 1 of Item 1250-011-0741, Budget Act of 2002 (Ch. 379, Stats. 2002), the $1,300,000 loan to the General Fund will be repaid in fiscal year 2012-13 upon order of the Director of Finance.

Vote:

2150 CALIFORNIA DEPARTMENT OF FINANCIAL INSTITUTIONS

Department Overview. The Department of Financial Institutions (DFI) was established effective July 1, 1997, to regulate depository institutions, including commercial banks, savings associations, credit unions, industrial loan companies, and certain other providers of financial services. In addition, the Department licenses and regulates issuers of payment instruments, including companies licensed to sell money orders and/or travelers' checks or licensed to engage in the business of transmitting money abroad, and business and industrial development corporations. Programs are supported by assessments of the various industries, license and application fees, and charges for various other services.

Budget Overview. The January Governor's Budget provides DFI with 250.2 authorized positions and $35 million (no GF). This is an increase of 2.7 positions and $55,000 over 2010-11.

Issues Proposed for Discussion / Vote:

Issue 1 – Problem Licensees: Banking Examination and Consumer Services Impact

Governor's Budget Request. The Governor requests:

1. Conversion of four limited-term positions to permanent status in the Banking Program; and
2. Three positions and $352,000 from special funds (including $50,000 contract funds) for the Consumer Services Program to address increased inquiries and complaints from the public resulting from the economic downturn.

Background. Each part of this request will be discussed separately.

Banking Program. The DFI Banking Program conducts examinations of financial institution loan portfolios, as mandated by state statute. These reviews are conducted on a risk-based examination schedule (but at least every 36 months). DFI works with financial institutions that are in trouble to return to a satisfactory condition and have adequate capital to operate and survive. Financial Institutions are rated on a scale of 1 to 5, with 1 representing the most financially sound bank. Currently, most of California's banks are rated 3 or worse. In 2009, DFI closed 11 banks and three credit unions in California.

Consumer Services Program. The Consumer Services Program receives complaints ranging from simple – overdraft fees, interest calculations, and car loans – to more complicated issues dealing with mortgage loans and modifications, missing funds, stocks, foreclosures, fraud, theft, and regulatory non-compliance. The Consumer Services Program received 620 complaints in 2007 and 1,744 complaints in 2010. However, during this time the number of staff available to respond to consumer complaints stayed the same. DFI is requesting three positions and $50,000 in contract funding to address the workload associated with the increased number and complexity of consumer complaints and inquiries.

Staff Comment. The Banking Program workload has rapidly increased since 2008 as the financial crisis stressed the resources of many banks and financial institutions. The Banking Program examiners take nearly three years to train for core understanding of the banking system. Not extending the four examiner positions would lead to a loss of valuable training time. Staff recommends that the state keep these four trained examiners since the workload for the department is continuing.

The Consumer Services Program workload has increased and additional positions to respond to the workload are justified. However, staff is skeptical that the volume of consumer complaints will hold as the economy begins to improve. Also, staff questions the need for the $50,000 in contract funds for consumer database maintenance. DFI already has a consumer database, and it is not clear why the maintenance costs of the database would have increased.

Staff Recommendation: Approve making permanent the four positions in the Banking Program. Approve Consumer Services Program positions as two-year limited-term positions. Reject the $50,000 in contract funds for the Consumer Services Program.

Vote:

2400 DEPARTMENT OF MANAGED HEALTH CARE

Department Overview. The Department of Managed Health Care (DMHC) was established in 2000, when the licensure and regulation of the managed health care industry was removed from the Department of Corporations and placed in a new, stand-alone, department. The mission of DMHC is to regulate, and provide quality-of-care and fiscal oversight for Health Maintenance Organizations (HMOs) and two Preferred Provider Organizations (PPOs). These 94 Health Care Plans provide health insurance coverage to approximately 64 percent of all Californians. Recent statutory changes also make DMHC responsible for the oversight of 240 Risk Bearing Organizations (RBOs), who actually deliver or manage a large proportion of the health care services provided to consumers. Within the Department, the Office of the Patient Advocate helps educate consumers about their HMO rights and responsibilities.

Budget Overview. The January Governor's Budget provides DFI with 250.2 authorized positions and $35 million (no GF). This is an increase of 2.7 positions and $55,000 over 2010-11.

Issues Proposed for Discussion / Vote:

Issue 1 – Senate Bill 1163 Premium Rate Review

Governor's Budget Request. The Governor requests 2.0 positions and $1,024,000 from the Managed Care Fund for FY 2011-12 and $908,000 for FY 2012-13 and ongoing (from the Managed Care Fund) to address new workload attributable to health plan rate increase review as specified in the federal Patient Protection and Affordable Care Act (PPACA or Health Care Reform) signed into law on March 23, 2010 and supported by Senate Bill 1163 enacted on September 30, 2010. Of the funds requested, $100,000 is one-time for an information technology consultant to assist with website design in accordance with public information disclosure requirements, and $600,000 is on-going for an external contract with an actuarial consultant.

Background. The Legislature passed, and the Governor signed, SB 1163 (Leno, 2010) to begin aligning California's laws with the federal Health Care Reform Act. With the passage of SB 1163, many of DMHC's roles and responsibilities for implementing Health Care Reform are defined and DMHC has been provided the authority to enforce the federal mandates in the state of California.

SB 1163 requires insurers to file rate information with DMHC that has been verified by an independent actuary under contract to the insurer. DMHC must make the rate information publicly available and verify rate information when it appears that a company may have violated the rate review process. DMHC must also provide information to the California Health Benefits Exchange and fulfill certain federal and state reporting requirements for health insurance rates.

Staff Comment. The workload associated with SB 1163 is new and thus there is uncertainty about the number of hours that will need to be devoted to the tasks DMHC is

required to undertake. Thus, staff thinks the requested positions should be made limited-term so that workload can be revisited in two years.

The funds for an external consultant to conduct actuarial review should be made limited-term (two-year) because it is not known what will be the actual workload. Also, DMHC should consider ways of bringing the actuarial review in-house rather than having a consultant contract indefinitely.

Staff Recommendation: Approve funds for two years and positions as two-year limited-term. Also, approve supplemental reporting language to have DMHC submit a report considering options for bringing actuarial review in-house.

Vote:

Senate Budget and Fiscal Review—Mark Leno, Chair

SUBCOMMITTEE NO. 4 Outcomes

Senator Michael J. Rubio, Chair
Senator Noreen Evans
Senator Doug La Malfa

Monday, February 7, 2011

Consultant: Seija Virtanen

PART B

Item Number and Title

1100	California Science Center
1110	Department of Consumer Affairs, Boards
1111	Department of Consumer Affairs, Bureaus
2150	Department of Financial Institutions
2400	Department of Managed Health Care

(See Table of Contents on page 2 for a More Specific Listing of Issues)

AGENDA – VOTE ONLY ITEMS

(Please see summary chart on Page 3)

AGENDA – DISCUSSION / VOTE ITEMS

Issues Proposed for Vote Only:

	Issue	2011-12 Amount	Fund Source	Staff Recommendation
	Department of Consumer Affairs, Boards (1110/1111)			
1	Board of Accountancy: Enforcement Division Staffing Augmentation	$0 (position authority only)	Special Funds	APPROVE
2	Physician Assistant Committee: Increase Reimbursement Authority	$25,000	Special Funds	APPROVE
3	State Board of Optometry: Staff Services Manager I Position	$0 (position authority only)	Special Funds	APPROVE
4	Various Bureaus: Baseline Funding Reduction	-$1.6 million combined	Various Special Funds	APPROVE
	Department of Managed Health Care (2400)			
5	Health Care Reform	$1.4 million	Special Funds	APPROVE

Vote: **Issues 1, 2, 3, 4 vote 2-0 (Evans)**
Issue 5 open

Issues Proposed for Vote Only – Issue Descriptions

DEPARTMENT OF CONSUMER AFFAIRS, BOARDS (1110)
DEPARTMENT OF CONSUMER AFFAIRS, BUREAUS (1111)

For overview and budget information regarding this department, please see page 10 of this agenda.

Issue 1 – Board of Accountancy: Enforcement Division Staffing Augmentation

Board of Accountancy. Created by statute in 1901, the California Board of Accountancy's legal mandate is to regulate the accounting profession for the public interest. To accomplish this, the Board qualifies California candidates for the National Uniform Certified Public Accountant (CPA) Examination; certifies, licenses, and renews licenses of individual CPAs and Public Accountants (PA); and registers CPA and PA partnerships and corporations; receives and investigates complaints; and takes enforcement actions against licensees for violation of Board statutes and regulations.

The Board of Accountancy currently regulates over 77,000 licensees, the largest group of licensed accounting professionals in the nation, including individuals, partnerships, and corporations.

The 2010-11 Budget for the Board of Accountancy is $12.21 million and 82.5 positions. The proposed 2011-12 Budget for the Board of Accountancy is $11.45 million and 85.8 positions. The Board of Accountancy's funding comes from fees paid by the licensees deposited into the Accountancy Fund.

Governor's Budget Request. The Governor requests position authority only for 2.5 Associate Governmental Program Analysts. The cost of these positions is $205,000 annually and will be redirected from excess funding authority in the Accountancy Fund.

Background. The Board of Accountancy's Enforcement Program currently has 17 positions. With a licensee population of 77,000, this equates to over 4,500 licensees per position. The Enforcement Program is responsible for investigations of complaints, probation monitoring, investigation of unlicensed activity, and verification of continuing education. In 2009-10 there were 682 complaints and an additional 67 cases of unlicensed activity. The Enforcement Program's average time for dealing with complaints is 249 days, but 46 cases have currently been open for more than a year. The new requested positions are intended to bring the timeframe for closing all cases down under 12 months.

Issue 2 – Physician Assistant Committee: Increase Reimbursement Authority

Physician Assistant Committee. The mission of the Physician Assistant Committee (PAC) of the Medical Board of California is to protect and serve consumers through licensing, education, and objective enforcement of the Physician Assistant laws and regulations. The PAC licenses and regulates physician assistants; enforces laws and regulations relating to physician assistant practice; encourages utilization of physician assistants in medically underserved areas; seeks ways and means to rehabilitate drug and alcohol impaired physician assistants; and encourages development of new physician assistant training programs and expansion of existing programs.

Governor's Budget Request. The Governor requests $25,000 in increased reimbursement authority for the PAC. The increased reimbursement authority would be used towards enforcement expenses that include investigation, attorney general, and probation monitor costs as intended.

Background. The reimbursements come primarily from applicant fingerprint fees and cost recovery ordered through disciplinary actions. Also, in 2007, the PAC began requiring licensees placed on probation to pay their probation monitoring costs. The reimbursement funds are placed in the Physician Assistant Fund, and cannot be spent unless there is reimbursement authority provided in the Budget Act.

During the last four years, PAC has collected between $10,000 and $46,000 more in reimbursements than it had authority to spend. If reimbursement authority is provided, but there are no funds in the account, the PAC would not be able to move expenditures forward.

In previous years, the PAC was forced to stop program activities during the last quarter of the fiscal year because its enforcement budget had been expended and the extra reimbursements from cost recovery and probation monitoring could not be used to offset enforcement costs.

Issue 3 – State Board of Optometry: Staff Services Manager I Position

State Board of Optometry. The California Legislature created the Board in 1913 to safeguard the public's health, safety, and welfare through regulation of the practice of optometry. Business and Professions Code section 3010.1 mandates the Board's highest priority as protection of the public. The State Board of Optometry is mandated to protect the public from the unauthorized and unqualified practice of optometry and from unprofessional conduct by persons licensed to practice optometry through its licensing, regulatory, and disciplinary functions.

Governor's Budget Request. The Governor requests position authority only for one Staff Services Manager I (SSMI) to serve as the Enforcement Manager. The position will cost $93,000 annually and will be funded by a redirection from Operating Expenses and Equipment from the State Optometry Fund.

Background. Currently, there are approximately 7,000 active optometric licensees in California and the state gains approximately 200 new licensees each year from new graduates and out-of state doctors seeking licensure in California. The increase in the licensee population over the years has led to a workload increase in administrative, licensing, and enforcement-related activities for Board staff, as well as an increase in the number of staff.

Supervising the increased workload has fallen on the Executive Officer (EO), which has resulted in extensive overtime and failing to meet various deadlines related to executive-level and supervisory tasks and responsibilities, e.g., completing Board minutes, probationary reports and individual development plans (IDPs), preparing progressive disciplinary counseling memos, drafting legislative proposals, and updating the Board's Strategic Plan. An SSM I would be able to assist the EO with the day-to-day supervision of staff, and oversee personnel, budget, and business service functions relating to enforcement activities within the Board.

Specifically, the SSM I would:
1. Provide day-to-day supervision;
2. Plan, organize, and direct the day-to-day work of clerical/analytical staff;
3. Hire/train new employees;
4. Complete probationary reports, annual reviews and individual Development Plans (IDPs), progressive disciplinary counseling memo;
5. Review and approve time-off requests; etc.

Issue 4 – Various Bureaus: Baseline Funding Reduction

Governor's Budget Request. The Governor requests a decrease in baseline funding authority for 2011-12 and on-going for the following programs:
1. Board of Accountancy: -$1,000,000
2. Architects Board: -$100,000
3. Board of Occupational Therapy: -$34,000
4. Bureau of Automotive Repair: -$500,000

Background. These Boards and Bureaus have consistently had reversions at the end of the fiscal year. This baseline funding reduction is a technical adjustment to bring funding authority in line with actual spending.

DEPARTMENT OF MANAGED HEALTH CARE (2400)

For overview and budget information regarding this department, please see page 19 of this agenda.

Issue 5 – Health Care Reform

Governor's Budget Request. The Governor requests $1,776,000 for 13.0 two-year limited-term positions to address new workload resulting from the March 2010 federal Health Care Reform Legislation.

Background. On March 23, 2010, President Obama signed into law comprehensive health care reform, the Patient Protection and Affordable Care Act, which was subsequently modified by the Health Care and Education Reconciliation Act of 2010 (hereinafter referred to as "Health Care Reform"). Health Care Reform will fundamentally alter the availability and structure of health insurance, bring coverage for the first time to millions of Californians, and bring new coverage options for millions of enrollees who receive care through California Knox-Keene Licensed health plans and contracted medical groups.

In light of the recent enactment of Health Care Reform, DMHC must take immediate action to assess and address the impacts of the reform on its mission critical operations. In response to Health Care Reform, DMHC will have to develop state regulations, review health plan documentation to comply with the new law, and respond to consumer inquiries.

The Department of Managed Health Care (DMHC) has explained that the positions are requested on a two-year limited-term basis not because DMHC expects the workload to be temporary, but to monitor the activity that results from Health Care Reform to determine if the workload assumptions hold true. Over the course of the two years, once all impacts are considered and a better assessment of new Health Care Reform workload results, the department will submit a future Budget Change Proposal to address the new permanent workload generated by the Health Care Reform legislation.

1100 CALIFORNIA SCIENCE CENTER

Department Overview. The California Science Center is an educational, scientific, and technological center located in Exposition Park, a 160-acre tract in south Los Angeles. The Science Center has interactive exhibits on human inventions and innovations, the life processes of living things, and temporary exhibits. The California African American Museum (CAAM), also included in the park, provides exhibitions and programs on the history, art, and culture of African Americans. In addition, the Office of the Park Manager is responsible for maintenance of the park, public safety, and parking facilities.

Budget Overview. The January Governor's Budget provides 190 authorized positions and $28.1 million ($19.4 million GF). It should be noted that the California Science Center budget includes the California African American Museum, Exposition Park Management, and facilities bond repayments. The reduction to the Science Center's operations is $3.66 million General Fund.

Issues Proposed for Discussion / Vote

Issue 1 – Unallocated Budget Reduction

Governor's Budget Request. The Governor requests an unallocated reduction of $3,660,000 to the Science Center's budget. The Governor also requests budget bill language to allow the Science Center to collect an admissions fee.

Background. The unallocated reduction of $3.7 million is 20 percent of the amount of General Fund remaining after excluding amounts budgeted for lease-revenue payments ($4.8 million). The General Fund base used for the calculation is $18.3 million ($23.1 million total General Fund less the $4.8 million).

The Science Center's operations have been based on the value that everyone is allowed access, and thus no admission fee has been charged. The Science Center does charge for parking and the IMAX movie tickets.

Staff Comment. Approximately one-third of the Science Center's visitors are school groups, which would be unlikely to afford admissions fees for each student, due to the funding restrictions that local school districts are currently experiencing.

Staff thinks that there are some possibilities for the Science Center to raise revenue that does not compromise the Science Center's dedication to free admission. The Science Center already charges $8 for parking, and $25 for parking at special events. (The Science Center also charges for their IMAX movie tickets.) It may be possible to raise additional revenue through increasing the parking fee from $8 to $10. The increase in parking fees would also apply to events at Exposition Park, including football games and concerts. Based on past Science Center parking fee increase revenue collections, staff estimates that the Science Center can collect approximately $800,000 in new revenue from raising parking fees.

The Office of the Exposition Park Management has an executive director appointed by the Governor for the purpose of managing, scheduling, and administering all park related events, including oversight for the police and security services of the park.

All items impacting the state of the General Fund will be heard in full committee.

Staff Recommendation: Staff recommends this issue be kept open for full committee consideration.

Vote: **No vote, issue held open**

1110/1111 DEPARTMENT OF CONSUMER AFFAIRS

Departmental Overview and Mission. The Department of Consumer Affair's (DCA) Boards and Bureaus provide exams and licensing, enforcement, complaint mediation, education for consumers, and information on privacy concerns. DCA Boards and Bureaus establish minimal competency standards for more than 255 professions involving approximately 2.4 million professionals. There are currently 25 boards, a commission, three committees, and eight bureaus under the broad authority of the DCA.

Budget Overview. The Boards are budgeted under organizational code 1110, and the total proposed budget is $271.46 million (no General Fund) and 1,511.3 positions – an increase of $10.4 million and 35.6 positions over 2010-11.

The Bureaus are budgeted under organizational code 1111, and the total proposed budget is $231.34 million (no General Fund) and 1,386.6 positions – an increase of $14.2 million and 5.7 positions over 2010-11.

DCA Boards and Bureaus

(dollars in thousands)

		Positions		Expenditures	
		2010-11	2011-12	2010-11	2011-12
1	Board of Accountancy	82.5	85.8	$ 12,210	$ 11,452
2	Architects Board	30.1	30.1	$ 4,686	$ 4,760
3	Athletic Commission	13.7	13.7	$ 2,541	$ 2,613
4	Board of Behavioral Science	42.6	43.4	$ 8,090	$ 7,898
5	Barbering and Cosmetology	95.1	95.1	$ 17,303	$ 18,291
6	Contractors State Licensing	402.1	402.1	$ 57,514	$ 59,979
7	Dental Board	71.6	75.1	$ 12,652	$ 13,496
8	Dental Hygiene Committee	6.2	6.7	$ 1,242	$ 1,358
9	Guide Dogs for the Blind	1.5	1.5	$ 180	$ 187
10	Medical Board	265.5	276.7	$ 52,385	$ 55,843
11	Acupuncture Board	7.9	8.0	$ 2,548	$ 2,603
12	Physical Therapy Board	15.0	16.4	$ 2,910	$ 3,290
13	Physician Assistant Com.	4.7	4.8	$ 1,387	$ 1,418
14	Podiatric Medicine	4.6	4.6	$ 1,362	$ 1,381
15	Psychology	15.3	18.3	$ 3,879	$ 4,335
16	Respiratory Care Board	15.9	16.1	$ 3,035	$ 3,138
17	Speech-Language Pathology	8.1	8.2	$ 1,848	$ 1,615
18	Occupational Therapy	10.5	10.2	$ 1,417	$ 1,473
19	Board of Optometry	10.9	11.1	$ 1,654	$ 1,574
20	Naturopathic Medicine Com.	0.9	0.9	$ 130	$ 141
21	Board of Pharmacy	75.4	80.0	$ 13,021	$ 14,448
22	Engineers and Land Surveyors	65.6	65.6	$ 10,397	$ 10,774
23	Registered Nursing	128.0	135.6	$ 28,250	$ 29,242
24	Court Reporters Board	4.3	4.3	$ 1,096	$ 1,114
25	Veterinary Medical Board	12.4	12.0	$ 2,639	$ 2,757
26	Vocational Nursing	74.7	73.3	$ 14,743	$ 14,237
27	Arbitration Certification Prog.	7.6	7.6	$ 1,098	$ 1,107
28	Hearing Aid Dispensers	0.0	0.0	$ -	$ -
29	Security and Investigative	50.2	50.7	$ 11,363	$ 11,865
30	Private Postsecondary Ed.	55.8	55.8	$ 10,160	$ 9,368
31	Electronic and Appliance Repair, Home Furnishings, and Thermal Insulation	41.9	41.9	$ 7,108	$ 7,781
32	Automotive Repair	596.2	600.2	$ 182,192	$ 195,798
33	Telephone Medical Advise Services Bureau	0.9	0.9	$ 145	$ 148
34	Cemetery and Funeral	21.2	18.5	$ 4,006	$ 4,149
35	Professional Fiduciaries	1.6	1.6	$ 282	$ 308

Issue Proposed for Discussion / Vote:

Issue 1 – Board of Accountancy: Peer Review Program

Governor's Budget Request. The Governor requests position authority only for one position to address clerical workload in the Board of Accountancy's Peer Review Program.

Background. Business and Professions Code Section 5076 requires that accounting firms providing audit, review, or compilation (accounting and auditing) services undergo a systematic review (peer review) of their accounting and auditing practice to ensure the work performed conforms to professional standards. Business and Professions Code Section 5035.1 defines a firm to be a sole proprietorship, a partnership, or a corporation. Peer review will be required every three years for accounting firms providing accounting and auditing services. This law became operative January 1, 2010, with the first group of accounting firms required to report peer review-related information no later than July 1, 2011.

The Board of Accountancy anticipates that approximately 6,000 accounting firms will be required to undergo a peer review, about 2,000 annually. The Board of Accountancy will be phasing in the accounting firm population over a three-year period, with the first group of accounting firms required to report specific peer review information no later than July 1, 2011. The Board of Accountancy will mail the peer review reporting form to all licensees with a current license once every three years.

In order to handle the volume of peer review reporting forms, the Board of Accountancy has determined that an additional Office Technician will be required to process the forms and be responsible for sending notifications to newly-licensed CPAs, along with other clerical duties. The Board of Accountancy anticipates that approximately five percent, or approximately 100 accounting firms yearly, will receive a substandard peer review rating, which requires submission of the peer review report by accounting firms. The Board of Accountancy also anticipates that beginning fiscal year 2011-12, 30 accounting firms will be referred to the Enforcement Division annually for failing to undergo a peer review, with increased referrals the following years. The Office Technician will assist with referral intake and provide some clerical support to Enforcement staff.

Staff Comment. The Board of Accountancy anticipates that only about half of the peer review reporting would take place electronically. If more licensees choose to file their peer reviews electronically, or if fewer firms are referred to the Enforcement Division than projected, there may be less workload and the need for an additional Office Technician will be reduced.

Staff Recommendation. Approve as a two-year limited-term position.

Vote: **Approved as two-year limited term position**
2-0 (Evans)

Issue 2 – Bureau of Automotive Repair: Consumer Assistance Program Funding Realignment and Augmentation

Bureau of Automotive Repair. The Bureau of Automotive Repair is responsible for regulating the automotive repair marketplace and administering the Smog Check Program. To carry out its mandate, the Bureau educates consumers, disciplines stations and technicians, seeks resolution to complaints, and licenses individuals and businesses. The Bureau also administers the nation's largest motor vehicle emissions reduction program.

Governor's Budget Request. The Governor requests $22.157 million and 12.3 positions from the Enhanced Fleet Modernization Subaccount in 2011-12 and ongoing. In addition, the Governor requests a reduction of $7.693 million and 8.0 positions from the High Polluter Repair or Removal Account.

Background. A key part of California's air quality emissions reduction strategy is to implement incentive-based air quality programs to encourage the early retirement and replacement of older vehicles with newer, cleaner ones. Older vehicles account for approximately 25 percent of the miles driven but contribute up to 75 percent of the emissions released. Reducing emissions from the older vehicles is a critical part of California's State Implementation Plan (SIP), which outlines the state's clean air strategy. The SIP is used by the federal government to determine the amount of federal transportation funds California will receive.

The Consumer Assistance Program (CAP) was started in 1997 and contains two parts: vehicle retirement and vehicle repair. Under the <u>vehicle repair</u> program, qualified low-income consumers can receive financial assistance of up to $500 to repair a vehicle that is unable to pass a biennial Smog Check inspection when it exceeds specified emission standards. To receive the repair assistance, eligible consumers must pay the initial $20 in repairs. Beginning in 2000, a directed vehicle repair program was started that allowed qualified consumers who owned a vehicle directed to a Test-Only or Gold Shield Smog Check station for an initial inspection to receive up to $500 in additional financial assistance toward emissions-related repairs after they paid the first $100 of repairs. Directed vehicles are identified by the Bureau of Automotive Repair.

Under the <u>vehicle retirement</u> program, until August 2010, consumers were paid $1,000 to retire a vehicle. These funds are not paid until after the vehicle is dismantled.

The passage of AB 787 (Hill, 2010) makes several additional changes to CAP. Under AB 787 the Bureau of Automotive Repair must offer all eligible low-income consumers an additional $500 to retire a vehicle through CAP. AB 787 also allows any vehicle that has been registered in California for two continuous years and has failed a lawfully required Smog Check inspection to be retired through CAP.

AB 787 also eliminates the provision of law authorizing owners of directed vehicles the ability to participate in the repair assistance option of CAP based solely on this designation and receive $500 toward emissions-related repairs.

Staff Comment. The expansion of the vehicle retirement program from a $1,000 payment to a $1,500 payment is anticipated to cost approximately $8 million annually in addition to the base costs of $14.1 million annually (for a total cost of about $22.1 million). The Bureau of Automotive Repair estimates that about 16,600 vehicles will be retired annually.

Savings result from the elimination of the directed vehicle part of the vehicle repair program. The Bureau of Automotive Repair data indicates that about 40 percent (or 18,682) of the vehicle repair eligible consumers participated in the directed vehicle program. The elimination of this program will lead to $7,603,600 in program savings and an additional $470,000 in administrative savings (total $8,073,600 in savings).

Staff Recommendation. Approve.

Vote: **No vote, issue held open**

Issue 3 – Various Boards and Bureaus: BreEZe

Governor's Budget Request. The Governor requests a realignment of existing BreEZe funding authority by $1.2 million in 2011-12. The funding is prior year funds that had not been spent. Previously, the Legislature had approved a schedule of funding with $2,283,000 for BreEZe in 2011-12, and this augmentation will bring the 2011-12 funding to $3,483,000.

The budget for BreEZe is as follows (years 2010-11 through 2014-15 total $20.3 million):

- 2010-11: $1,330,000 (redirected from existing resources)
- 2011-12: $3,483,000
- 2012-13: $3,600,000
- 2013-14: $6,219,000
- 2014-15 and ongoing: $6,125,000

Background. Licensing of businesses and professionals includes: processing applications and qualifying applicants, conducting exams/processing results, maintaining and analyzing licensing-related information, authorizing practice(s) and issuing licensing documents, renewing licenses, performing Family Support verification, creating a variety of management reports, and processing a multitude of other requests.

The BreEZe system will bring all of the DCA boards and bureaus into an integrated licensing and enforcement system. In addition, the licensees will be able to use the BreEZe system to renew their licenses and update their addresses on-line. Currently, the 40 boards and bureaus do not have integrated systems (so a person could hold a medical license and a pharmacy assistant license and it would not be known to the enforcement units). BreEZe will allow for secure cross-license checking for every DCA board and bureau, and provide the ability to interface with any other capable external systems used in the enforcement process, such as the Department of Justice, the Employment Development Department, or the Department of Public Health, once the appropriate agreements have been established authorizing the secured sharing of the data.

The DCA Office of Information Services has an Office of the Chief Information Officer approved Feasibility Study Report (FSR) proposal for the BreEZe project.

The DCA has structured the BreEZe cost proposal based on a "fee-per-transaction" payment model. Under this payment model, the solution vendor receives no payment prior to the State's acceptance and use of the production system. Instead, the solution vendor will be compensated by assessing system clients with a transaction fee for specific master transactions. For the BreEZe system, the DCA is anticipating that the solution vendor will assess a $3 per transaction fee to boards and bureaus for each new application or $0.50 for each renewal processed through the new system.

The BreEZe Request for Proposals (RFP) was released in May 2010, and was met with concerns from bidders that the proposed payment model was overly burdensome and would limit the bidders' ability to submit proposals to the state. DCA wants to change the RFP to provide a $1.2 million payment for the solution software following installation of the software on State equipment, and the State's acceptance of the detailed solution design.

Staff Comment. Last year the Legislature requested a report on staffing workload needs once the BreEZe system is completed. The BreEZe system should be able to expedite the license renewal process and reduce the amount of paperwork that must be manually processed. The Legislature also requested a copy of the final vendor contract in order to ensure that costs remain reasonable.

Since the BreEZe system will automate much of the licensing renewal process it can potentially create great savings for the DCA boards and bureaus. Delays in contracting would also delay the actualization of these savings.

This augmentation does not increase the overall project costs, but rather takes current year unspent funds and offers them as a bidding incentive.

Staff Recommendation. Approve.

Vote: **Approved**
2-0 (Evans)

Issue 4 – Board of Accountancy and Dental Board: Loan Repayment

Dental Board of California. The Dental Board of California establishes minimal standards of competency for those individuals seeking to practice as a dentist, registered dental hygienist, registered dental assistant, dental auxiliary in extended function, or dental hygienist in alternative practice. The Board enforces standards to protect California dental consumers from incompetent dental practitioners, and the utilization of dental auxiliaries contributes to providing quality dental services to Californians.

Effective January 1, 2009, the State Dental Assistant Committee (Committee) was created and assumed the duties of the Committee on Dental Auxiliaries with regard to dental assistants, pursuant to Chapter 31, Statutes of 2008 (SB 853).

Governor's Budget Request. The Governor requests repayment of two loans from the General Fund to special funds: 1) $10 million repayment by the General Fund to the Accountancy Fund, and 2) $2.5 million repayment by the General Fund to the State Dentistry Fund.

Background. During the 2010-11 fiscal year, the State loaned $10 million from the Accountancy Fund to the General Fund. This amount is set to be repaid in June 2012.

During the 2002-03 fiscal year, the State loaned $2.5 million from the State Dentistry Fund to the General Fund. This amount is set to be repaid in June 2012.

Staff Comment. The Accountancy Fund loan repayment can be delayed by one year without having an influence on the Board's programs.

$1.3 million of the loan from the State Dentistry Fund can be delayed by one year without having an influence on the Board's programs.

Staff Recommendation. Delay repayment of the Accountancy Fund $10 million loan until June 30, 2013. Include the following budget bill language:

Add Item 1110-404:
1110-404—Notwithstanding Provision 1 of Item 1110-011-0704, Budget Act of 2010 (Ch. 712, Stats. 2010), the $10,000,000 loan to the General Fund will be repaid in fiscal year 2012-13 upon order of the Director of Finance.

Delay repayment of $1.3 million of the State Dentistry Fund loan repayment until June 30, 2013. Include the following budget bill language:

Add Item 1110-405:
1110-405—Notwithstanding Provision 1 of Item 1250-011-0741, Budget Act of 2002 (Ch. 379, Stats. 2002), the $1,300,000 loan to the General Fund will be repaid in fiscal year 2012-13 upon order of the Director of Finance.

Vote: **No vote, issue held open**

2150 CALIFORNIA DEPARTMENT OF FINANCIAL INSTITUTIONS

Department Overview. The Department of Financial Institutions (DFI) was established effective July 1, 1997, to regulate depository institutions, including commercial banks, savings associations, credit unions, industrial loan companies, and certain other providers of financial services. In addition, the Department licenses and regulates issuers of payment instruments, including companies licensed to sell money orders and/or travelers' checks or licensed to engage in the business of transmitting money abroad, and business and industrial development corporations. Programs are supported by assessments of the various industries, license and application fees, and charges for various other services.

Budget Overview. The January Governor's Budget provides DFI with 250.2 authorized positions and $35 million (no GF). This is an increase of 2.7 positions and $55,000 over 2010-11.

Issues Proposed for Discussion / Vote:

Issue 1 – Problem Licensees: Banking Examination and Consumer Services Impact

Governor's Budget Request. The Governor requests:

1. Conversion of four limited-term positions to permanent status in the Banking Program; and
2. Three positions and $352,000 from special funds (including $50,000 contract funds) for the Consumer Services Program to address increased inquiries and complaints from the public resulting from the economic downturn.

Background. Each part of this request will be discussed separately.

Banking Program. The DFI Banking Program conducts examinations of financial institution loan portfolios, as mandated by state statute. These reviews are conducted on a risk-based examination schedule (but at least every 36 months). DFI works with financial institutions that are in trouble to return to a satisfactory condition and have adequate capital to operate and survive. Financial Institutions are rated on a scale of 1 to 5, with 1 representing the most financially sound bank. Currently, most of California's banks are rated 3 or worse. In 2009, DFI closed 11 banks and three credit unions in California.

Consumer Services Program. The Consumer Services Program receives complaints ranging from simple – overdraft fees, interest calculations, and car loans – to more complicated issues dealing with mortgage loans and modifications, missing funds, stocks, foreclosures, fraud, theft, and regulatory non-compliance. The Consumer Services Program received 620 complaints in 2007 and 1,744 complaints in 2010. However, during this time the number of staff available to respond to consumer complaints stayed the same. DFI is requesting three positions and $50,000 in contract funding to address the workload associated with the increased number and complexity of consumer complaints and inquiries.

Staff Comment. The Banking Program workload has rapidly increased since 2008 as the financial crisis stressed the resources of many banks and financial institutions. The Banking Program examiners take nearly three years to train for core understanding of the banking system. Not extending the four examiner positions would lead to a loss of valuable training time. Staff recommends that the state keep these four trained examiners since the workload for the department is continuing.

The Consumer Services Program workload has increased and additional positions to respond to the workload are justified. However, staff is skeptical that the volume of consumer complaints will hold as the economy begins to improve. Also, staff questions the need for the $50,000 in contract funds for consumer database maintenance. DFI already has a consumer database, and it is not clear why the maintenance costs of the database would have increased.

Staff Recommendation: Approve making permanent the four positions in the Banking Program. Approve Consumer Services Program positions as two-year limited-term positions. Reject the $50,000 in contract funds for the Consumer Services Program.

Vote: **Approved staff recommendation**
2-0 (Evans)

2400 DEPARTMENT OF MANAGED HEALTH CARE

Department Overview. The Department of Managed Health Care (DMHC) was established in 2000, when the licensure and regulation of the managed health care industry was removed from the Department of Corporations and placed in a new, stand-alone, department. The mission of DMHC is to regulate, and provide quality-of-care and fiscal oversight for Health Maintenance Organizations (HMOs) and two Preferred Provider Organizations (PPOs). These 94 Health Care Plans provide health insurance coverage to approximately 64 percent of all Californians. Recent statutory changes also make DMHC responsible for the oversight of 240 Risk Bearing Organizations (RBOs), who actually deliver or manage a large proportion of the health care services provided to consumers. Within the Department, the Office of the Patient Advocate helps educate consumers about their HMO rights and responsibilities.

Budget Overview. The January Governor's Budget provides DFI with 250.2 authorized positions and $35 million (no GF). This is an increase of 2.7 positions and $55,000 over 2010-11.

Issues Proposed for Discussion / Vote:

Issue 1 – Senate Bill 1163 Premium Rate Review

Governor's Budget Request. The Governor requests 2.0 positions and $1,024,000 from the Managed Care Fund for FY 2011-12 and $908,000 for FY 2012-13 and ongoing (from the Managed Care Fund) to address new workload attributable to health plan rate increase review as specified in the federal Patient Protection and Affordable Care Act (PPACA or Health Care Reform) signed into law on March 23, 2010 and supported by Senate Bill 1163 enacted on September 30, 2010. Of the funds requested, $100,000 is one-time for an information technology consultant to assist with website design in accordance with public information disclosure requirements, and $600,000 is on-going for an external contract with an actuarial consultant.

Background. The Legislature passed, and the Governor signed, SB 1163 (Leno, 2010) to begin aligning California's laws with the federal Health Care Reform Act. With the passage of SB 1163, many of DMHC's roles and responsibilities for implementing Health Care Reform are defined and DMHC has been provided the authority to enforce the federal mandates in the state of California.

SB 1163 requires insurers to file rate information with DMHC that has been verified by an independent actuary under contract to the insurer. DMHC must make the rate information publicly available and verify rate information when it appears that a company may have violated the rate review process. DMHC must also provide information to the California Health Benefits Exchange and fulfill certain federal and state reporting requirements for health insurance rates.

Staff Comment. The workload associated with SB 1163 is new and thus there is uncertainty about the number of hours that will need to be devoted to the tasks DMHC is

required to undertake. Thus, staff thinks the requested positions should be made limited-term so that workload can be revisited in two years.

The funds for an external consultant to conduct actuarial review should be made limited-term (two-year) because it is not known what will be the actual workload. Also, DMHC should consider ways of bringing the actuarial review in-house rather than having a consultant contract indefinitely.

Staff Recommendation: Approve funds for two years and positions as two-year limited-term. Also, approve supplemental reporting language to have DMHC submit a report considering options for bringing actuarial review in-house.

Vote: **No vote, issue held open**

SUBCOMMITTEE NO. 4 Agenda

Senator Michael J. Rubio, Chair
Senator Doug LaMalfa
Senator Noreen Evans

Agenda – Part A

Thursday, February 10, 2011
9:30 a.m. or upon adjournment of session
Room 112

Consultant: Brian Annis

Item Number and Title **Page**

Proposed Discussion / Vote Issues:

(See Table of Contents on page 1 for a more specific listing of issues)

Pursuant to the Americans with Disabilities Act, individuals who, because of a disability, need special assistance to attend or participate in a Senate Committee hearing, or in connection with other Senate services, may request assistance at the Senate Rules Committee, 1020 N Street, Suite 255 or by calling 916-324-9335. Requests should be made one week in advance whenever possible.

AGENDA – DISCUSSION / VOTE ITEMS

Issues Suggested for Discussion / Vote:

0520 Secretary for Business, Transportation and Housing

Department Overview: The Secretary of the Business, Transportation and Housing Agency (BT&H Agency) is a member of the Governor's Cabinet and oversees 16 departments, including the following large departments:

- Alcoholic Beverage Control
- Corporations
- Housing and Community Development
- California Highway Patrol
- Motor Vehicles
- Financial Institutions
- Real Estate
- Managed Health Care
- Transportation

In addition, the Secretary's Office oversees programs, including the following, which are budgeted directly in the Secretary's Office:

- Infrastructure and Economic Development Bank
- Film Commission
- Small Business Loan Guarantee Program
- Tourism Commission

Budget Overview: The Governor proposes total expenditures of $100.9 million ($4.2 million General Fund) and 60.7 positions for the Office of the Secretary – an increase of $78.2 million from the adjusted 2010-11 budget, and an increase of 1.5 funded positions. The primary reason for the year-over-year change is a one-time federal grant of $84.4 million to support the Small Business Loan Guarantee Program.

(See budget issue on next page)

Issue 1 – Small Business Loan Guarantee Program Expansion (BCP #2)

Governor's Budget Request. The Governor requests various budget changes related to a federal grant award that will result in one-time funding of $84.4 million for the Small Business Loan Guarantee Program (SBLG). This represents a significant expansion of the program which has typically had a trust-fund balance between $30 million and $40 million. The SBLG Program provides assistance to small businesses that may not qualify for traditional loans, by guaranteeing a portion of the loaned amount. The Administration requests to revert $20 million in General Fund support provided to the program one-time as part of the 2010 Budget Act (AB 1632, Chapter 731, Statutes of 2010). This reversion of $20 million is contingent on receipt of the federal funds. Finally, the Administration requests to double program staff from 1.5 positions to 3.0 positions.

Background / Detail. The Small Business Loan Guarantee Program is administered by 11 non-profit Financial Development Corporations (FDCs) via contracts with the State. In the current year, administration funding for the FDCs sum about $2.2 million ($1.7 million General Fund and $500,000 interest earnings) and the cost of the state oversight positions is about $150,000 (General Fund). The FDCs additionally charge fees in the range of 1 – 3 percent on the loan guarantees – which, with the federal money, could provide administration funding of the magnitude of $5 million depending on the volume of guarantees. The trust fund itself currently has a balance of about $44 million, and loan guarantees must not exceed five times the balance of the trust fund. In recent years, the SBLG Program has experienced significant fluctuation in General Fund support, trust fund earnings, and even a temporary suspension in new loan activities due to a prior reversion to the General Fund. The $84 million in federal funds would support the program at a new peak level, and would arrive in three parts over time – about $28 million should be received by the end of 2010-11.

Staff Comment: The federal funds allow the state to expand this program, which is popular in many communities, and at the same time realize a General Fund benefit of $20 million by reverting the augmentation provided last year. This baseline proposal appears to be a "win-win" for the program and State General Fund. The budget question that may merit consideration of the Subcommittee is what level of staffing is appropriate, and can additional General Fund relief be realized from substituting these new federal funds for base program funding and trust fund balances. Specifically:

- Can the state perform program oversight with fewer than 3.0 positions?
- Can the base $1.9 million General Fund support for state administration and the FDCs, be reduced or deleted and backfilled with federal funds?
- Can the base trust fund balance of $24 million be reverted to the General Fund immediately, or over time, and backfilled with federal funds?

LAO Recommendation: The Analyst recommends the Legislature:
a) Adopt the Governor's proposal to revert $20 million to the General Fund.

b) Adopt trailer bill language (TBL) to allow for the reversion of the additional General Fund dollars as the lines of credit and loans backed by roughly $24 million in state funds expire.
c) Reduce the request for additional staff by one and approve the 0.5 managerial position.
d) Consider eliminating the $1.7 million General Fund subsidy provided to FDCs.

Staff Recommendation:

a) Adopt the Governor's proposal (and LAO recommendation) to revert $20 million to the General Fund.
b) Reject LAO recommendation to adopt TBL to revert base trust fund assets (about $24 million) to the General Fund, but adopt TBL to direct that new loan guarantees use federal funds first.
c) Adopt the LAO recommendation to approve 0.5 new staff instead of 1.5 new staff.
d) Reject LAO recommendation to eliminate General Fund support for administration, and rather convert program administration funding to 50-percent General Fund and trust fund interest, and 50-percent federal funds, which is proportional to new program resources. (In the out-years, the administration funding share could be adjusted again to reflect program resources after the full federal grant is received. This staff recommendation would provide additional FDC administration funding over the base level for ramp-up, but still result in General Fund expenditure savings of about $1.0 million).

Vote:

8880 Financial Information System for California

Department Overview: The Financial Information System for California (FI$Cal), is an Enterprise Resource Planning (ERP) information technology (IT) project intended to replace, consolidate, and upgrade multiple legacy financial systems with a single system that would encompass the areas of: budgeting; accounting; procurement; cash management; and financial management. The development of FI$Cal resides with four "Partner Agencies": the Department of Finance, the State Treasurer's Office, the State Controller's Office, and the Department of General Services. The FI$Cal system will be implemented in several phases, or "waves," over the next decade. Budget Control Section 8.88 is a technical fiscal provision that directs special funds to the FI$Cal project and it will be made to conform to the final budget adopted under the 8880 budget items.

Budget Overview: The Governor proposes $70.8 million ($20.9 million General Fund) for continuing the FI$Cal project. This represents a year-over-year increase of $29.0 million ($5.2 million General Fund). Funded positions would grow from 62.1 to 95.9. The reason for the funding increase is that the project would be moving into the implementation stage with contract award to the vendor by December 31, 2011. The 12-year cost of fully implementing the project is estimated at $1.6 billion (both General Fund and other funds). The Administration is exploring financing options such as bonding and vender-financing to spread costs over a longer period.

(See budget issue on next page)

Issue 1 – FI$Cal Budget Request for 2011-12 (BCP #1)

Governor's Budget Request: As indicated above, the Governor requests $70.8 million ($20.9 million General Fund) for the project in 2011-12. The next 12 months are a critical time for the project, with key decision points on whether to move forward with the project as currently configured, how to finance the project, and to which vendor to award the integration contract. Current law (Government Code 15849.21) requires a report to the Legislature and 90-day review by the Joint Legislature Budget Committee (JLBC), after a contract is negotiated with the winning bidder, but prior to contract award – this report is anticipated in the July to September period of this year.

Project Timeline: Currently, three selected vendors are completing the "Fit-Gap," or stage I contract, which involves a review of potential gaps between the vendor's software and the state's business requirements. Project staff have also asked the three vendors to propose financing options and have held discussions with the State Infrastructure Bank (I-Bank) on financing options. The following are key upcoming dates:

- February 2011 – Financing proposals due from vendors.
- March 2011 – Fit-Gap or Stage I proposals due and begin negotiations.
- July 2011 – Select winning contractor and proceed on final negotiations.
- August 2011 – Deliver Special Project Report #4 and report to JLBC. The JLBC report is required to include costs and benefits of alternative approaches to the implementation of the FI$Cal system, including, but not limited to, a scaled-back version of the system.
- December 2011 (or earlier) – Award contract.
- January 2012 – Ramp up project and costs - $20 million for contractor, $12.7 for State Office of Technology Service, hire 33 new positions, and other activities included in the BCP.

Staff Comments: As the timeline above indicates, there will be new information and legislative reporting coming over the next few months and in the late summer / early fall. Some of this information will be available as the Subcommittee continues with budget hearings in April and May. Other information will only come after the budget is passed and the new fiscal year begins on July 1. Due to this schedule, the Subcommittee may wish to consider holding final action on the FI$Cal budget until later this spring. Because the report to the Legislature will not arrive until after the budget is passed, the Legislature will want to carefully consider budget bill language, or trailer bill language, to maintain appropriate legislative funding control after the proposed-contract detail is provided.

Staff Recommendation: Hold open for future consideration in the spring after further detail is available on alternative financing options.

California Alternative Energy and Advanced Transportation Financing Authority (0971)

Department Overview: The mission of the California Alternative Energy and Advanced Transportation Financing Authority (CAEATFA) is to promote the prompt and efficient development of energy sources which are renewable or which more efficiently utilize and conserve scarce energy resources.

Budget Overview: The January Governor's Budget proposed total funding of $25.8 million (special funds and reimbursements) and 7.0 positions, an increase of $9.2 million and no change in positions. The year-over-year increase is primarily explained by the implementation of California Ethanol Producers Incentive Program (See Issue 1 on the following page for detail on this budget request).

Informational Note on the PACE Program: Due to a continuous appropriation enacted last year, the CAEATFA budget includes a $15 million transfer from the Renewable Resource Trust Fund related to the Property Assessed Clean Energy Program (PACE). The PACE Program provides up-front financing for renewable and energy efficiency-related upgrades to properties with a unique financing mechanism of a loan that is backed by the property and transferable to new owners if the property changes hands. Recent state legislation, SB 77 (Chapter 15, Statutes of 2010, Pavley), facilitated program participation by small local governments by allowing them to pool PACE bonds via CAEATFA before going to market. The federal government has recently determined that the PACE program presents significant safety and soundness concerns that must be addressed by Fannie Mae, Freddie Mac, and the Federal Home Loan Banks. The federal action effectively halted the operation of PACE programs while the legal issues now proceed to the courts. The Legislative Analyst recommends that the Legislature reverse the $15 million transfer, without prejudice, pending legal resolution of the issue that has suspended PACE activity. Staff suggests no action at this time, as the PACE issue may be addressed in a policy bill, or may be better informed by review in Budget Subcommittee #2 which oversees energy-related budget issues. This Subcommittee can revisit this issue at a later date as warranted.

(See budget issue on next page)

Issue 1 – AB 118 / Ethanol Producers Incentive Program (BCP#1)

Governor's Request: The Administration requests $9 million in reimbursement authority for CAEATFA to receive funds from the California Energy Commission (CEC) to perform activities related to the Alternative and Renewable Fuel and Vehicle Technology Program as authorized by AB 118 (Chapter 750, Statutes of 2007, Nunez). The specific program is the California Ethanol Producer Incentive Program whereby financial assistance is provided to ethanol producers selected by CEC to develop and commercialize advanced transportation technologies that meet advanced energy goals.

Background/Detail: AB 118 authorizes the CEC to implement various programs consistent with the most recently adopted Investment Plan for the Alternative and Renewable Fuel and Vehicle Technology Program. Pursuant to the 2010 Budget Act, CAEATFA and the CEC are entering into an interagency agreement that outlines the terms by which CAEATFA will assist CEC in implementing the ethanol incentive program goals. The interagency agreement is expected to have a 4-year term expiring in January 2015. The terms of the agreement require CEC to transfer a total of $15 million.

Staff Comment: The Governor's budget reflects a $15 million reimbursement in 2010-11 and a $9 million reimbursement in in the budget year. The two-year amount requested exceeds the interagency agreement by about $9 million – CAEATFA indicates this is proposed due to uncertainty about how funds will be distributed across fiscal years and to maximize flexibility.

LAO Recommendation: The Legislative Analyst recommends holding action on this item pending receipt of the 2011-12 AB 118 Investment Plan, which should be submitted to the Legislature this March. The Legislature has expressed a great deal of interest in the AB 118 program administered by CEC, and as such, has statutorily required that the CEC annually submit an AB 118 Investment Plan. This requirement is designed to improve the Legislature's oversight of the AB 118 program.

Staff Recommendation: Deny without prejudice to defer final consideration of this request to later this spring after the AB 118 report has been provided and reviewed.

Vote:

9620 Cash Management and Budgetary Loans

Department Overview: This budget item appropriates funds to pay interest costs on General Fund borrowing used to overcome cash flow imbalances during the fiscal year. Because receipts and disbursements occur unevenly throughout the fiscal year, the General Fund borrows in most years, even though each budget is balanced when enacted and funds are repaid within the fiscal year. Interest is paid on both internal borrowing (such as cashflow loans from special funds) and for external borrowing (such as Revenue Anticipation Notes [RANs]). This item additionally pays interest costs for budgetary borrowing by the General Fund from special funds. Budgetary borrowing is across fiscal years and is scored as a budget solution, whereas cashflow borrowing is not counted as a budget solution (only a cash solution).

Budget Overview: The January Governor's Budget includes $300 million for interest costs on cashflow borrowing and $62 million for interest costs on budgetary borrowing – all General Fund. Of the cashflow amount, $100 million is for internal borrowing and $200 million is for external borrowing. Overall, expenditures in this item are up significantly – a total of $362 million is proposed for 2011-12, versus revised expenditures of $230 million in 2010-11. The year-over-year difference is primarily explained by the late budget last year that delayed the RAN sale until late in 2010. The Administration assumes the 2011-12 RAN sale will occur in July, resulting in a longer borrowing period and higher interest costs.

(see budget issues on next page)

Issue 1 – Intra-year Payment Deferrals / Cashflow Loans (Trailer Bill Language)

Governor's Proposal: The Administration requests statutory change that would allow intra-year cash payment deferrals in 2011-12, which would be similar to the authority granted for 2010-11. These deferrals represent an additional cashflow solution that have been necessary even after internal and external cashflow borrowing. The language also allows cashflow loans from two additional funds: the Immediate and Critical Needs Account in the State Court Facilities Construction Fund and the Hospital Quality Assurance Revenue Fund.

Background: Last year's cashflow measures were enacted by three bills: AB X8 5; AB X8 14; and AB 1624. The 2010-11 legislation provided approximately $5 billion in cashflow relief, and this year's proposal would be reduced to about $4.5 billion, due to the prohibition placed on borrowing from certain transportation funds by Proposition 22 of 2010. Last year's deferral plan was developed in consultation with higher education and local governments to minimize negative consequences. Finally, the plan includes triggers, such that the deferrals will not occur if the team of the State Treasurer, the State Controller, and the Director of Finance concur they are not necessary to maintain cash balances for the State. Cashflow loans are allowed for most special funds and existing statute requires repayment as needed for the program.

Detail: As indicated above, the Governor's proposal for 2011-12 is very similar to the enacted plan for 2010-11. The following are the major statutory components:

- K-12 Education – Permits up to 3 deferral periods not to exceed $2.5 billion at any one time. Includes a hardship-exemption process for certain local education agencies.
- Community College – Permits deferrals up to $200 million.
- California State University – permits deferrals up to $250 million.
- Cities and Counties – permits deferrals of specified payments to local governments not to exceed $1 billion.

Through existing administrative authority (no statutory change needed), the Administration could also defer $500 million to the University of California and about $81 million of CalWORKs administrative funding to counties.

Staff Comment: The Department of Finance should explain the need for the cash deferrals in 2011-12 and explain how the 2011-12 plan would compare and contrast to the 2010-11 plan. While cash deferrals to other government units are not desirable, they appear necessary for 2011-12 to avoid payment deferrals to private vendors and taxpayers (such as vendor payments and delayed tax refunds).

Staff Recommendation: Approve the placeholder trailer bill language.

Vote:

Issue 2 – Repayment of Special Fund Loans (Governor's Budget)

Governor's Proposal: As indicated in the introduction to this issue, the January Governor's Budget requests $62 million General Fund to pay interest on outstanding special-fund loans – this is budgeted in item 9620. Interest is only repaid when the loan principal is repaid. The amount of principal repaid is $566 million; however, principal repayment is budgeted as a revenue adjustment instead of an expenditure. The amount of total special fund loans outstanding as of December 31, 2010, is $2.6 billion, according to the Department of Finance. This table below reflects the Administration's planned special-fund loan repayments in 2011-12 (dollars in millions).

Fund Name	Principal	Interest
Accountancy Fund	$10,000,000	$84,521
Contractors' License Fund	10,000,000	727,003
State Dentistry Fund	3,000,000	739,688
Occupational Therapy Fund	640,000	79,627
Enhanced Fleet Modernization Subaccount	20,000,000	169,041
Public School Planning, Design, and Construction Review Revolving Fund	10,000,000	727,003
Housing Rehabilitation Loan Fund	9,200,000	965,526
Rental Housing Construction Fund	500,000	72,762
State Highway Account, State Transportation Fund	200,000,000	19,566,247
Bicycle Transportation Account, State Transportation Fund	6,000,000	586,987
Local Airport Loan Account	7,500,000	733,734
Motor Vehicle Fuel Account, Transportation Tax Fund	8,000,000	782,650
Environmental Enhancement and Mitigation Program Fund	4,400,000	430,457
Historic Property Maintenance Fund	3,000,000	293,494
Pedestrian Safety Account, State Transportation Fund	1,715,000	167,781
Motor Vehicle Account	40,000,000	338,082
Beverage Container Recycle Fund	88,000,000	21,697,524
Tire Recycling Management Fund	27,097,000	2,914,531
Recycling Market Development Revolving Loan Subaccount	1,853,000	248,918
Universal Lifeline Telephone Service Trust Administrative Committee Fund	45,000,000	3,271,512
Deaf and Disabled Telecommunications Program Administrative Committee Fund	30,000,000	2,181,008
Teleconnect Fund	40,000,000	5,373,288
	$565,905,000	**$62,151,384**

Staff Comment: The Department of Finance should present their special-fund loan repayment plan and the LAO should comment. Generally, decisions about special fund loans will be made in the budget Subcommittees by subject-matter area, although the 9620 Budget Item should be made to conform.

Governor's February 9, 2011, Budget Revision: On February 9, 2011, Governor Brown canceled the sale-leaseback of 11 state office buildings and proposed to backfill for the General Fund loss with new special fund loans, repayment deferrals, and other measures. The new solutions total $1.2 billion. Full detail on that proposal was not available at the time this agenda was finalized, but staff has asked the Department of Finance to present a summary of the revised plan at the hearing.

Staff Recommendations: Take no action, this is an informational issue.

Senate Budget and Fiscal Review— Mark Leno, Chair

SUBCOMMITTEE NO. 4 Agenda

Senator Michael J. Rubio, Chair
Senator Doug LaMalfa
Senator Noreen Evans

Agenda – Part A

Hearing Outcomes

Thursday, February 10, 2011
9:30 a.m. or upon adjournment of session
Room 112

Consultant: Brian Annis

Item Number and Title **Page**

Proposed Discussion / Vote Issues:

(See Table of Contents on page 1 for a more specific listing of issues)

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AGENDA – DISCUSSION / VOTE ITEMS

Issues Suggested for Discussion / Vote:

0520 Secretary for Business, Transportation and Housing

Department Overview: The Secretary of the Business, Transportation and Housing Agency (BT&H Agency) is a member of the Governor's Cabinet and oversees 16 departments, including the following large departments:

- Alcoholic Beverage Control
- Corporations
- Housing and Community Development
- California Highway Patrol
- Motor Vehicles
- Financial Institutions
- Real Estate
- Managed Health Care
- Transportation

In addition, the Secretary's Office oversees programs, including the following, which are budgeted directly in the Secretary's Office:

- Infrastructure and Economic Development Bank
- Film Commission
- Small Business Loan Guarantee Program
- Tourism Commission

Budget Overview: The Governor proposes total expenditures of $100.9 million ($4.2 million General Fund) and 60.7 positions for the Office of the Secretary – an increase of $78.2 million from the adjusted 2010-11 budget, and an increase of 1.5 funded positions. The primary reason for the year-over-year change is a one-time federal grant of $84.4 million to support the Small Business Loan Guarantee Program.

(See budget issue on next page)

Issue 1 – Small Business Loan Guarantee Program Expansion (BCP #2)

Governor's Budget Request. The Governor requests various budget changes related to a federal grant award that will result in one-time funding of $84.4 million for the Small Business Loan Guarantee Program (SBLG). This represents a significant expansion of the program which has typically had a trust-fund balance between $30 million and $40 million. The SBLG Program provides assistance to small businesses that may not qualify for traditional loans, by guaranteeing a portion of the loaned amount. The Administration requests to revert $20 million in General Fund support provided to the program one-time as part of the 2010 Budget Act (AB 1632, Chapter 731, Statutes of 2010). This reversion of $20 million is contingent on receipt of the federal funds. Finally, the Administration requests to double program staff from 1.5 positions to 3.0 positions.

Background / Detail. The Small Business Loan Guarantee Program is administered by 11 non-profit Financial Development Corporations (FDCs) via contracts with the State. In the current year, administration funding for the FDCs sum about $2.2 million ($1.7 million General Fund and $500,000 interest earnings) and the cost of the state oversight positions is about $150,000 (General Fund). The FDCs additionally charge fees in the range of 1 – 3 percent on the loan guarantees – which, with the federal money, could provide administration funding of the magnitude of $5 million depending on the volume of guarantees. The trust fund itself currently has a balance of about $44 million, and loan guarantees must not exceed five times the balance of the trust fund. In recent years, the SBLG Program has experienced significant fluctuation in General Fund support, trust fund earnings, and even a temporary suspension in new loan activities due to a prior reversion to the General Fund. The $84 million in federal funds would support the program at a new peak level, and would arrive in three parts over time – about $28 million should be received by the end of 2010-11.

Staff Comment: The federal funds allow the state to expand this program, which is popular in many communities, and at the same time realize a General Fund benefit of $20 million by reverting the augmentation provided last year. This baseline proposal appears to be a "win-win" for the program and State General Fund. The budget question that may merit consideration of the Subcommittee is what level of staffing is appropriate, and can additional General Fund relief be realized from substituting these new federal funds for base program funding and trust fund balances. Specifically:

- Can the state perform program oversight with fewer than 3.0 positions?
- Can the base $1.9 million General Fund support for state administration and the FDCs, be reduced or deleted and backfilled with federal funds?
- Can the base trust fund balance of $24 million be reverted to the General Fund immediately, or over time, and backfilled with federal funds?

LAO Recommendation: The Analyst recommends the Legislature:
a) Adopt the Governor's proposal to revert $20 million to the General Fund.

b) Adopt trailer bill language (TBL) to allow for the reversion of the additional General Fund dollars as the lines of credit and loans backed by roughly $24 million in state funds expire.
c) Reduce the request for additional staff by one and approve the 0.5 managerial position.
d) Consider eliminating the $1.7 million General Fund subsidy provided to FDCs.

Staff Recommendation:
a) Adopt the Governor's proposal (and LAO recommendation) to revert $20 million to the General Fund.
b) Reject LAO recommendation to adopt TBL to revert base trust fund assets (about $24 million) to the General Fund, but adopt TBL to direct that new loan guarantees use federal funds first.
c) Adopt the LAO recommendation to approve 0.5 new staff instead of 1.5 new staff.
d) Reject LAO recommendation to eliminate General Fund support for administration, and rather convert program administration funding to 50-percent General Fund and trust fund interest, and 50-percent federal funds, which is proportional to new program resources. (In the out-years, the administration funding share could be adjusted again to reflect program resources after the full federal grant is received. This staff recommendation would provide additional FDC administration funding over the base level for ramp-up, but still result in General Fund expenditure savings of about $1.0 million).

Action: On a 3 – 0 vote, adopted the staff recommendation, but additionally adopted budget bill language that would allow the Director of Finance to transfer up to $20 million from the GF to the Trust Fund if loan defaults reduce the trust fund balance to the extent additional funds are necessary to maintain a 5:1 reserve ratio for outstanding loans. Joint Legislative Budget Committee (JLBC) notification would be required.

8880 Financial Information System for California

Department Overview: The Financial Information System for California (FI$Cal), is an Enterprise Resource Planning (ERP) information technology (IT) project intended to replace, consolidate, and upgrade multiple legacy financial systems with a single system that would encompass the areas of: budgeting; accounting; procurement; cash management; and financial management. The development of FI$Cal resides with four “Partner Agencies”: the Department of Finance, the State Treasurer's Office, the State Controller's Office, and the Department of General Services. The FI$Cal system will be implemented in several phases, or “waves,” over the next decade. Budget Control Section 8.88 is a technical fiscal provision that directs special funds to the FI$Cal project and it will be made to conform to the final budget adopted under the 8880 budget items.

Budget Overview: The Governor proposes $70.8 million ($20.9 million General Fund) for continuing the FI$Cal project. This represents a year-over-year increase of $29.0 million ($5.2 million General Fund). Funded positions would grow from 62.1 to 95.9. The reason for the funding increase is that the project would be moving into the implementation stage with contract award to the vendor by December 31, 2011. The 12-year cost of fully implementing the project is estimated at $1.6 billion (both General Fund and other funds). The Administration is exploring financing options such as bonding and vender-financing to spread costs over a longer period.

(See budget issue on next page)

Issue 1 – FI$Cal Budget Request for 2011-12 (BCP #1)

Governor's Budget Request: As indicated above, the Governor requests $70.8 million ($20.9 million General Fund) for the project in 2011-12. The next 12 months are a critical time for the project, with key decision points on whether to move forward with the project as currently configured, how to finance the project, and to which vendor to award the integration contract. Current law (Government Code 15849.21) requires a report to the Legislature and 90-day review by the Joint Legislature Budget Committee (JLBC), after a contract is negotiated with the winning bidder, but prior to contract award – this report is anticipated in the July to September period of this year.

Project Timeline: Currently, three selected vendors are completing the "Fit-Gap," or stage I contract, which involves a review of potential gaps between the vendor's software and the state's business requirements. Project staff have also asked the three vendors to propose financing options and have held discussions with the State Infrastructure Bank (I-Bank) on financing options. The following are key upcoming dates:

- February 2011 – Financing proposals due from vendors.
- March 2011 – Fit-Gap or Stage I proposals due and begin negotiations.
- July 2011 – Select winning contractor and proceed on final negotiations.
- August 2011 – Deliver Special Project Report #4 and report to JLBC. The JLBC report is required to include costs and benefits of alternative approaches to the implementation of the FI$Cal system, including, but not limited to, a scaled-back version of the system.
- December 2011 (or earlier) – Award contract.
- January 2012 – Ramp up project and costs - $20 million for contractor, $12.7 for State Office of Technology Service, hire 33 new positions, and other activities included in the BCP.

Staff Comments: As the timeline above indicates, there will be new information and legislative reporting coming over the next few months and in the late summer / early fall. Some of this information will be available as the Subcommittee continues with budget hearings in April and May. Other information will only come after the budget is passed and the new fiscal year begins on July 1. Due to this schedule, the Subcommittee may wish to consider holding final action on the FI$Cal budget until later this spring. Because the report to the Legislature will not arrive until after the budget is passed, the Legislature will want to carefully consider budget bill language, or trailer bill language, to maintain appropriate legislative funding control after the proposed-contract detail is provided.

Staff Recommendation: Hold open for future consideration in the spring after further detail is available on alternative financing options.

Action: No action taken. Issue to be considered further in the spring.

California Alternative Energy and Advanced Transportation Financing Authority (0971)

Department Overview: The mission of the California Alternative Energy and Advanced Transportation Financing Authority (CAEATFA) is to promote the prompt and efficient development of energy sources which are renewable or which more efficiently utilize and conserve scarce energy resources.

Budget Overview: The January Governor's Budget proposed total funding of $25.8 million (special funds and reimbursements) and 7.0 positions, an increase of $9.2 million and no change in positions. The year-over-year increase is primarily explained by the implementation of California Ethanol Producers Incentive Program (See Issue 1 on the following page for detail on this budget request).

Informational Note on the PACE Program: Due to a continuous appropriation enacted last year, the CAEATFA budget includes a $15 million transfer from the Renewable Resource Trust Fund related to the Property Assessed Clean Energy Program (PACE). The PACE Program provides up-front financing for renewable and energy efficiency-related upgrades to properties with a unique financing mechanism of a loan that is backed by the property and transferable to new owners if the property changes hands. Recent state legislation, SB 77 (Chapter 15, Statutes of 2010, Pavley), facilitated program participation by small local governments by allowing them to pool PACE bonds via CAEATFA before going to market. The federal government has recently determined that the PACE program presents significant safety and soundness concerns that must be addressed by Fannie Mae, Freddie Mac, and the Federal Home Loan Banks. The federal action effectively halted the operation of PACE programs while the legal issues now proceed to the courts. The Legislative Analyst recommends that the Legislature reverse the $15 million transfer, without prejudice, pending legal resolution of the issue that has suspended PACE activity. Staff suggests no action at this time, as the PACE issue may be addressed in a policy bill, or may be better informed by review in Budget Subcommittee #2 which oversees energy-related budget issues. This Subcommittee can revisit this issue at a later date as warranted.

(See budget issue on next page)

Issue 1 – AB 118 / Ethanol Producers Incentive Program (BCP#1)

Governor's Request: The Administration requests $9 million in reimbursement authority for CAEATFA to receive funds from the California Energy Commission (CEC) to perform activities related to the Alternative and Renewable Fuel and Vehicle Technology Program as authorized by AB 118 (Chapter 750, Statutes of 2007, Nunez). The specific program is the California Ethanol Producer Incentive Program whereby financial assistance is provided to ethanol producers selected by CEC to develop and commercialize advanced transportation technologies that meet advanced energy goals.

Background/Detail: AB 118 authorizes the CEC to implement various programs consistent with the most recently adopted Investment Plan for the Alternative and Renewable Fuel and Vehicle Technology Program. Pursuant to the 2010 Budget Act, CAEATFA and the CEC are entering into an interagency agreement that outlines the terms by which CAEATFA will assist CEC in implementing the ethanol incentive program goals. The interagency agreement is expected to have a 4-year term expiring in January 2015. The terms of the agreement require CEC to transfer a total of $15 million.

Staff Comment: The Governor's budget reflects a $15 million reimbursement in 2010-11 and a $9 million reimbursement in in the budget year. The two-year amount requested exceeds the interagency agreement by about $9 million – CAEATFA indicates this is proposed due to uncertainty about how funds will be distributed across fiscal years and to maximize flexibility.

LAO Recommendation: The Legislative Analyst recommends holding action on this item pending receipt of the 2011-12 AB 118 Investment Plan, which should be submitted to the Legislature this March. The Legislature has expressed a great deal of interest in the AB 118 program administered by CEC, and as such, has statutorily required that the CEC annually submit an AB 118 Investment Plan. This requirement is designed to improve the Legislature's oversight of the AB 118 program.

Staff Recommendation: Deny without prejudice to defer final consideration of this request to later this spring after the AB 118 report has been provided and reviewed.

Action: Denied budget request without prejudice to defer final consideration to spring budget hearings.

9620 Cash Management and Budgetary Loans

Department Overview: This budget item appropriates funds to pay interest costs on General Fund borrowing used to overcome cash flow imbalances during the fiscal year. Because receipts and disbursements occur unevenly throughout the fiscal year, the General Fund borrows in most years, even though each budget is balanced when enacted and funds are repaid within the fiscal year. Interest is paid on both internal borrowing (such as cashflow loans from special funds) and for external borrowing (such as Revenue Anticipation Notes [RANs]). This item additionally pays interest costs for budgetary borrowing by the General Fund from special funds. Budgetary borrowing is across fiscal years and is scored as a budget solution, whereas cashflow borrowing is not counted as a budget solution (only a cash solution).

Budget Overview: The January Governor's Budget includes $300 million for interest costs on cashflow borrowing and $62 million for interest costs on budgetary borrowing – all General Fund. Of the cashflow amount, $100 million is for internal borrowing and $200 million is for external borrowing. Overall, expenditures in this item are up significantly – a total of $362 million is proposed for 2011-12, versus revised expenditures of $230 million in 2010-11. The year-over-year difference is primarily explained by the late budget last year that delayed the RAN sale until late in 2010. The Administration assumes the 2011-12 RAN sale will occur in July, resulting in a longer borrowing period and higher interest costs.

(see budget issues on next page)

Issue 1 – Intra-year Payment Deferrals / Cashflow Loans (Trailer Bill Language)

Governor's Proposal: The Administration requests statutory change that would allow intra-year cash payment deferrals in 2011-12, which would be similar to the authority granted for 2010-11. These deferrals represent an additional cashflow solution that have been necessary even after internal and external cashflow borrowing. The language also allows cashflow loans from two additional funds: the Immediate and Critical Needs Account in the State Court Facilities Construction Fund and the Hospital Quality Assurance Revenue Fund.

Background: Last year's cashflow measures were enacted by three bills: AB X8 5; AB X8 14; and AB 1624. The 2010-11 legislation provided approximately $5 billion in cashflow relief, and this year's proposal would be reduced to about $4.5 billion, due to the prohibition placed on borrowing from certain transportation funds by Proposition 22 of 2010. Last year's deferral plan was developed in consultation with higher education and local governments to minimize negative consequences. Finally, the plan includes triggers, such that the deferrals will not occur if the team of the State Treasurer, the State Controller, and the Director of Finance concur they are not necessary to maintain cash balances for the State. Cashflow loans are allowed for most special funds and existing statute requires repayment as needed for the program.

Detail: As indicated above, the Governor's proposal for 2011-12 is very similar to the enacted plan for 2010-11. The following are the major statutory components:

- K-12 Education – Permits up to 3 deferral periods not to exceed $2.5 billion at any one time. Includes a hardship-exemption process for certain local education agencies.
- Community College – Permits deferrals up to $200 million.
- California State University – permits deferrals up to $250 million.
- Cities and Counties – permits deferrals of specified payments to local governments not to exceed $1 billion.

Through existing administrative authority (no statutory change needed), the Administration could also defer $500 million to the University of California and about $81 million of CalWORKs administrative funding to counties.

Staff Comment: The Department of Finance should explain the need for the cash deferrals in 2011-12 and explain how the 2011-12 plan would compare and contrast to the 2010-11 plan. While cash deferrals to other government units are not desirable, they appear necessary for 2011-12 to avoid payment deferrals to private vendors and taxpayers (such as vendor payments and delayed tax refunds).

Staff Recommendation: Approve the placeholder trailer bill language.

Action: Approved the Administration's placeholder trailer bill language.

Issue 2 – Repayment of Special Fund Loans (Governor's Budget)

Governor's Proposal: As indicated in the introduction to this issue, the January Governor's Budget requests $62 million General Fund to pay interest on outstanding special-fund loans – this is budgeted in item 9620. Interest is only repaid when the loan principal is repaid. The amount of principal repaid is $566 million; however, principal repayment is budgeted as a revenue adjustment instead of an expenditure. The amount of total special fund loans outstanding as of December 31, 2010, is $2.6 billion, according to the Department of Finance. This table below reflects the Administration's planned special-fund loan repayments in 2011-12 (dollars in millions).

Fund Name	Principal	Interest
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	$565,905,000	**$62,151,384**

Staff Comment: The Department of Finance should present their special-fund loan repayment plan and the LAO should comment. Generally, decisions about special fund loans will be made in the budget Subcommittees by subject-matter area, although the 9620 Budget Item should be made to conform.

Governor's February 9, 2011, Budget Revision: On February 9, 2011, Governor Brown canceled the sale-leaseback of 11 state office buildings and proposed to backfill for the General Fund loss with new special fund loans, repayment deferrals, and other measures. The new solutions total $1.2 billion. Full detail on that proposal was not available at the time this agenda was finalized, but staff has asked the Department of Finance to present a summary of the revised plan at the hearing.

Staff Recommendations: Take no action, this is an informational issue.

Action: Informational – no action taken.

9100 Tax Relief

Action: On a 3 – 0 vote, rejected the Governor's proposal for Williamson Act open-space subventions, and funded at the $20 million level in 2011-12. (Funding of $10 million restored for 2010-11.)

Senate Budget and Fiscal Review—Mark Leno, Chair

SUBCOMMITTEE NO. 4 Agenda

Senator Michael J. Rubio, Chair
Senator Noreen Evans
Senator Doug LaMalfa

Thursday, February 10, 2011
9:30 a.m. or Upon Adjournment of Session
Room 112

Consultant: Kris Kuzmich

OPEN ISSUES – ALL DEPARTMENTS

AGENDA PART B

Item Number and Title

0840	State Controller's Office
1700	Department of Fair Employment and Housing
1760	Department of General Services
8855	Bureau of State Audits
8860	Department of Finance; California Recovery Task Force State Operations Efficiencies

(See Table of Contents on page 2 for a More Specific Listing of Issues)

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AGENDA – VOTE ONLY ITEMS

(Please see summary chart on Page 3)

AGENDA – DISCUSSION / VOTE ITEMS

Issue Proposed for Vote Only:

	Issue	2011-12 Amount	Fund Source	Staff Recommendation
	Bureau of State Audits (8855)			
1	Budget Augmentation	$8.2 million and 34 positions	$4.7 million GF $3.5 million Central Service Cost Recovery Fund	APPROVE

Vote:

Issues Proposed for Vote Only – Issue Descriptions

BUREAU OF STATE AUDITS (8855)

For overview and budget information regarding this department, please see the Subcommittee's February 7, 2011, agenda.

Issue 1 – Budget Augmentation

Prior Subcommittee Action. At its February 7, 2011, hearing, the Subcommittee held this item open pending receipt of additional information.

Governor's Budget Request. The State Auditor requests an increase of $8.2 million ($4.7 million GF) and 34 positions in 2011-12 to fund a two-year plan to better assist the Legislature in its oversight of government operations, including conducting additional audits, completing more high risk analyses, and better integrating the audit process with the work of legislative budget and policy committees.

Background. Currently, the Auditor has 147 employees on staff. In Year 1 of this plan, the Auditor proposes to increase staffing by 34 positions, to a total of 181 positions. In Year 2, an additional 37 staff would be added, bringing staffing to a total of 218 positions. In Year 1, the Auditor reports that it will utilize $3.5 million of the requested funding to contract with outside experts to conduct the federal compliance audit work, thereby allowing the Auditor to utilize the remaining $4.5 million to recruit, hire, and train the 34 new in-house staff to conduct the additional mandated, discretionary, and high-risk audit work as well as investigations. These 34 staff will also respond to increases in other activities, such as inquiries and requests from legislative staff, legal assistance, and public record requests, due to the additional audits being completed. In Year 2, the Auditor reports that it should have a sufficient number of trained audit and investigative staff to conduct the increase in audit work and provide the additional integration with legislative oversight. Consequently, in Year 2, the Auditor plans to substantially reduce or eliminate the contracted federal compliance work to hire the additional 37 staff.

At the end of the two-year plan, which will result in the addition of 54 new audit staff, the Auditor reports that audit production will increase from the 2010-11 average of 30 audits per year, to 50-55 per year, including discretionary and mandated audits, as well as more work under the high-risk authority. The additional audit staff will also reduce the time it currently takes to complete an audit, and will also reduce staff burnout and a high turnover rate. The Auditor reports that the addition of eight investigative staff over the two years will result in self-initiated statewide investigations increasing from the 2010-11 average of one per year to four to eight per year.

The Auditor indicates that the additional audit and investigative results from the two-year plan will produce more monetary benefits for the state, and offers the following recent examples of savings from audit and investigative work: (1) $194 million in unallowable costs, plus $53 million in cost avoidance over seven years (State Mandates Audits, 2003 and 2009); (2) $3.3 million revenue increase (Citation Penalty Accounts, 2010-108); (3) $4.8 million in cost avoidance (Medi-Cal TARS, 2009-112); and (4) $12 million cost recovery (CalWorks, 2009-101).

0840 STATE CONTROLLER'S OFFICE (SCO)

For overview and budget information regarding this department, please see the Subcommittee's January 25, 2011, agenda.

Issue Proposed for Discussion / Vote:

Issue 1 – Unclaimed Property Legal Costs

Prior Subcommittee Action. This issue was held open at the Subcommittee's January 25, 2011, hearing pending receipt of additional information from the SCO.

Governor's Budget Request. The Governor requests a two-year augmentation of $300,000 (Unclaimed Property Fund) beginning in 2011-12 to provide representation in legal matters associated with representing the Unclaimed Property Program in lawsuits filed against the SCO.

Background. Under current law, the SCO is responsible for safeguarding unclaimed property until it is returned to its rightful owner. Claims processed through the Unclaimed Property Program are paid, returned for insufficient information, or denied. When a claim is denied, claimants are notified of their right to commence an action against the SCO pursuant to law. When these actions are taken, the SCO has 60 days to respond. In addition to these actions by individual claimants, other actions, including class action type suits in both state and federal court have been brought against the SCO. These suits allege the program is unconstitutional, claiming the SCO has not properly administered the program and is not seeking restitution for plaintiffs.

The Attorney General normally represents the SCO, but the SCO reports that the Attorney General does not have the resources to respond to all of the actions brought against the SCO. The SCO is requesting the additional funds for a limited amount of time to clear the existing lawsuits for only the most complex cases; the SCO views this as more cost effective than hiring permanent staff and training them for what may eventually result in a lack of workload. The SCO reports that it will be in a better position in two years to gauge the volume and complexity of lawsuits and perhaps the need for permanent staff, whether at the SCO or the Attorney General's Office.

Staff Comment. The resources in this request are to continue the use of outside counsel for two pre-existing class action lawsuits. Over the life of these lawsuits, the Attorney General's Office has approved the use of outside counsel. Staff concurs with the SCO's assessment that to change counsel midstream in these cases would not be prudent. Staff also notes that this request is a two-year limited-term increase in expenditure authority.

Staff Recommendation: Approve the budget request.

Vote:

1700 DEPARTMENT OF FAIR EMPLOYMENT AND HOUSING (DFEH)
1760 DEPARTMENT OF GENERAL SERVICES (DGS)

For overview and budget information regarding these departments, please see the Subcommittee's January 27, 2011, agenda.

Issue Proposed for Discussion / Vote:

Issue 1 – Information Technology Transfer to Department of General Services; Retain Two Positions for Enforcement

Prior Subcommittee Action. At its January 27, 2011, hearing, the Subcommittee: (1) approved the transfer of the DFEH IT function and workload to DGS; (2) swept the excess five positions at DGS as well as the $300,000 Service Revolving Fun; and (3) left open the DFEH requests to retain the two positions for enforcement and provide reimbursement to DGS for the transferred IT functions.

Governor's Budget Request. The Governor requests to permanently transfer DFEH's Information Technology (IT) function and five positions to the Department of General Services (DGS) and proposes budget provisional language that sets aside $507,000 GF from DFEH to pay for the transferred functions. In addition, the Governor proposes to redirect the two remaining IT positions to DFEH's enforcement division on a two-year limited-term basis to process claims resulting from the settlement of a class-action lawsuit.

Background. The DFEH entered into an agreement with the DGS effective July 2010 which transferred DFEH's entire IT function and five positions to DGS's IT unit and provided $465,000 to DGS for the cost of providing these services in 2010-11. One objective of this agreement was to achieve efficiency and cost savings.

In September 2010, DFEH reached its first multi-million dollar discrimination settlement, totaling more than $6.9 million. According to the DFEH, the settlement will result in a significant increase in workload. The DFEH, therefore, is proposing to retain the two remaining IT positions and convert them into two-year limited-term positions in its Special Investigations Unit to address expected new workload stemming from the settlement of 1,500 family leave claims. All claims are required to be submitted by February 15, 2011. Shortly thereafter, the designated third-party administrator will submit all timely and valid claim forms to DFEH and DFEH staff will then conduct an independent evaluation of each claim to determine whether, on a case-by-case basis, the claimant experienced a California Family Rights Act violation and, if so, the type of violation and the appropriate level of damages.

Staff Comment. When the Subcommittee initially considered this issue at its January 27, 2011, hearing, concerns were expressed that workload justifications had not been provided for: (1) DFEH to retain two positions for enforcement; and (2) DFEH to provide reimbursement to DGS for the cost of DGS providing IT functions to DFEH. These justifications are necessary; otherwise, the resources provided could be greater than is warranted.

Since that hearing, both DGS and DFEH have provided the requested workload justifications. With regard to the number of claims received under the class action lawsuit, DFEH is on track to receive the requisite number to justify the retention of the two positions on a two-year limited-term basis.

With regard to the transfer of DFEH's IT function to DGS, staff notes that this is the first time the DGS IT unit is taking on a transferred IT function under contract for another state department. Given that, staff recommends that this portion of the request also be made two-year limited-term to allow this transfer to be revisited and reexamined in two-year's time to determine if DFEH has seen a reduction in its costs by having DGS provide its IT function.

Staff Recommendation. Approve on a two-year limited-term basis the request for DFEH to: (1) retain two positions for enforcement activities and (2) provide reimbursement to DGS for the transferred IT function.

Vote:

8860 DEPARTMENT OF FINANCE (DOF), CALIFORNIA RECOVERY TASK FORCE

For overview information regarding the California Recovery Task Force, please see the Subcommittee's January 27, 2011, agenda.

Issue Proposed for Discussion / Vote:

Issue 1 – California Recovery Task Force – ARRA Funds Oversight

Prior Subcommittee Action. This issue was held open at the Subcommittee's January 27, 2011, hearing pending receipt of additional information.

Governor's Budget Request. The Governor requests one-time funds totaling $1.6 million ($928,000 GF and $700,000 Central Service Cost Recovery Fund) to support oversight and reporting for remaining ARRA funds in 2011-12. In addition to supporting the California Recovery Task Force (CRTF), the resources in this request will also provide funding for the California Technology Agency (CaTA) and support staff at Department of Finance [Office of State Audits and Evaluations (OSAE) and Fiscal Systems Consulting Unit (FSCU)], providing information technology activities related to federally-required quarterly reports and continued audit support, respectively. Figure 1 below illustrates funding levels for the three entities comprising the CRTF generally:

Figure 1

	2010-11	**2011-12 Funding**
California Recovery Task Force	$1,700,000	$578,000
California Technology Agency	$1,400,000	$600,000
Department of Finance: (1) Office of State Audits and Evaluations; and, (2) Fiscal Systems Consulting Unit	$905,000	$450,000
TOTAL	**$4,005,000**	**$1,628,000**

**Note, the fund split is 57 percent GF and 43 percent Central Service Cost Recovery Fund.*

Background. The primary functions that remain in 2011-12 will be quarterly reporting, compliance monitoring, and ensuring that all deadlines related to retaining ARRA funds are met to avoid losing any money awarded due to failure to spend funds within the required timeframes or for other non-compliance issues. CRTF responsibilities diminish as funds are expended; therefore, this proposal significantly reduces the staffing of the CRTF to oversee the remaining ARRA funds and to provide continued quarterly reports. In September 2010, 1,121 ARRA grants remained; in 2011-12, that number will drop to 568 grants.

The CaTA is responsible for ongoing maintenance of the California ARRA and Accountability Tool (CAAT), the state's centralized reporting database. The CAAT tool provides a vehicle for departments to submit and report the data, but is only one component of the information technology (IT) required to report the information to the federal government and citizens of the state. In 2011-12, the CaTA will transition from contract/consultant staff on the CAAT system to utilization of state staff. The State IT staff will fully support and maintain the IT infrastructure (hardware, software, and connectivity), the multitude of user accounts, and provide end-user support for the ongoing reporting. Currently, there are over 300 registered users uploading over 1,100 reports consisting of thousands of records to the system in multiple formats. There will be savings realized in 2011-12 as the maintenance and support is transitioned from contractor resources to state staff; however, CAAT requires continuous support and maintenance due to the complexity of the system and the continued reporting to the federal government. The funding for position support will be absorbed within the CaTA.

Staff Comment. The proposed resources for the CRTF in 2011-12 have been reduced from the level provided in 2010-11 reflective of the declining workload. However, staff notes that this request proposes five positions for the CRTF itself and 4.9 borrowed staff from the Department of Finance. Staff finds that this level of staffing is still greater than needed to meet the reduced workload which now consists primarily of recipient reporting to the CAAT which is administered by the CaTA. Therefore, the Subcommittee may wish to further reduce the proposed staffing levels for the CRTF in 2011-12 by instead providing three positions for the CRTF itself to complete required ARRA workload and three borrowed positions from DOF to continue to provide a reduced audit/oversight role. Should the Subcommittee adopt this recommendation, the request would be decreased by $393,000 ($224,000 GF and $169,000 Central Service Cost Recovery Fund).

Staff Recommendation: Approve the request but reduce the 2011-12 resources for the California Recovery Task Force by $393,000 ($224,000 GF and $169,000 Central Service Cost Recovery Fund), including a reduction of two CRTF positions and $150,000 to reflect reduced OSAE support.

Vote:

STATE OPERATIONS EFFICIENCIES

Governor's Budget Request. The January Governor's Budget includes $363 million ($200 million GF) in savings associated with identification of efficiencies in state operations; review of state peace officer and safety classifications; and reductions in other areas such as contracting, fleet operations, and cell phone use. The mechanism to achieve these savings is Control Section 3.91, which requires the Director of Finance to allocate the reductions necessary to each item of appropriation in the budget to accomplish the required savings.

Prior Subcommittee Action. This issue was heard as an informational item at the Subcommittee's January 25, 2011, hearing with testimony focused on a January 11, 2011, Executive Order (EO) that requires cell phone usage to be reduced by 50 percent for savings of at least $20 million (all funds). Since that time, the Administration has: (1) issued an additional EO related to Fleet Management; and (2) identified savings in both 2010-11 and 2011-11 due to a reduction in Department of General Services' (DGS) building rental rates.

Issue Proposed for Discussion

Issue 1 - Fleet Management

Background. On January 28, 2011, Governor Brown issued an EO requiring that: (1) the state passenger car and truck fleet, comprised of approximately 11,000 non-public safety vehicles, be reduced by 50 percent; and (2) home storage permits, which currently total 4,500 (excluding public health and safety) and allow state employees to use passenger cars for their daily commute, be reduced by 50 percent. The EO requires that underutilized vehicles be moved to new locations, so that the state fleet will be more efficient overall, and requires all vehicles deemed "non-essential" be sold or transferred within 120 days of an approved analysis and plan for vehicle allocation/retention. The EO prohibits agencies and departments from buying new vehicles for non-emergency use. Finally, this EO supersedes the prior Administration's July 2009 EO on fleet management which required a reduction of the overall size of the fleet by at least 15 percent and a reduction of home vehicle storage permits by at least 20 percent.

Staff Comment. Presently, the Administration does not have a savings estimate attached to the EO. That information will likely become available after March 1, 2011, which is the date that departments and agencies are required to report into DOF the results of their internal review of their current fleet and home storage permits.

Committee Questions. Based on the above information, the Committee may wish the Administration to provide responses to the following questions:

1. How does this EO interact with the prior Administration's EO? Was that prior EO not fully implemented, so new reductions of 50 percent are achievable?
2. The state vehicle fleet is actually much larger than the 11,000 figure noted in the EO because public safety vehicles are excluded. Is the Administration certain that all of the vehicles used by public safety are in use and there no efficiencies to be gained?

Staff Recommendation. None; informational item only.

Issue Proposed for Discussion / Vote:

Issue 2 – Reduction in Department of General Services' Building Rental Rates

Governor's Request. The Governor requests uncodified trailer bill language to authorize the Director of Finance to reduce 2010-11 appropriations to reflect a reduction in the building rental rates charged to departments by the Department of General Services (DGS).

Background. DGS charges building rental rates for state owned buildings that fall into one of two categories: (1) Building Rental Account Buildings – no debt service; and (2) Individual Rate Buildings – with debt service. In both categories, the DGS charged rate is for costs to support and maintain the building, such as janitorial services and building maintenance. For buildings in the Individual Rate Building category, debt service costs are added to the cost to support and maintain the building.

The DGS has determined that its rental rates will decrease substantially in 2010-11 and 2011-12. More specifically, DGS has determined that the cost for Building Rental Account Buildings is decreasing from $1.80/square foot to $1.40/square foot in 2010-11 and to $1.12/square foot in 2011-12. The Individual Rate Buildings are also decreasing with varying costs depending on the building. Overall, the 2010-11 savings total an estimated $31.3 million and the 2011-12 savings total an estimated $27.5 million. DOF is continuing to work on an estimate of the fund splits (GF versus other funds); departmental input is necessary for a more precise estimate as DGS does not have that level of funding information.

Staff Comment. Generally speaking, the 40 cent decrease in the rate DGS is charging agencies and departments in 2010-11 is translating to reduced current year costs for those entities (and reduced levels of reimbursements for DGS). The decrease in 2010-11 is related to employee compensation savings, primarily from nine furlough days and the workforce cap which reduced personnel costs across all departments by five percent ongoing. The DOF reports that it can reduce most departmental budgets using the existing 2010 budget act authority contained in Control Section 3.90(b). However, there are a number of entities that are exempt from these provisions, many of which would have GF savings, including the courts, Franchise Tax Board, and Board of Equalization, as well as the constitutional officers. To capture the savings associated with these rate reductions, the Administration requests uncodified trailer bill language that authorizes the Director of Finance to reduce appropriations to reflect a reduction in the building rental rates charged to departments by DGS.

For 2011-12, the DOF has determined that Control Section 3.91, which relates to State Operations Efficiencies, provides the authority needed to capture these savings.

Staff concurs that additional authority is needed in the current year to ensure that all of these savings are captured.

Staff Recommendation. Approve trailer bill language to authorize the Administration to reduce appropriations in 2010-11 to reflect a reduction in building rental rates charged to departments by DGS.

Vote:

Senate Budget and Fiscal Review—Mark Leno, Chair

SUBCOMMITTEE NO. 4 Agenda

Senator Michael J. Rubio, Chair
Senator Noreen Evans
Senator Doug LaMalfa

Thursday, February 10, 2011
9:30 a.m. or Upon Adjournment of Session
Room 112

Consultant: Kris Kuzmich

OPEN ISSUES – ALL DEPARTMENTS

AGENDA PART B

OUTCOMES

Item Number and Title

0840	State Controller's Office
1700	Department of Fair Employment and Housing
1760	Department of General Services
8855	Bureau of State Audits
8860	Department of Finance; California Recovery Task Force State Operations Efficiencies

(See Table of Contents on page 2 for a More Specific Listing of Issues)

Pursuant to the Americans with Disabilities Act, individuals who, because of a disability, need special assistance to attend or participate in a Senate Committee hearing, or in connection with other Senate services, may request assistance at the Senate Rules Committee, 1020 N Street, Suite 255 or by calling 916-324-9335. Requests should be made one week in advance whenever possible.

AGENDA – VOTE ONLY ITEMS

(Please see summary chart on Page 3)

AGENDA – DISCUSSION / VOTE ITEMS

Issue Proposed for Vote Only:

	Issue	2011-12 Amount	Fund Source	Staff Recommendation
	Bureau of State Audits (8855)			
1	Budget Augmentation	$8.2 million and 34 positions	$4.7 million GF $3.5 million Central Service Cost Recovery Fund	APPROVE

Vote: Budget request approved by a 3-0 vote.

Issues Proposed for Vote Only – Issue Descriptions

BUREAU OF STATE AUDITS (8855)

For overview and budget information regarding this department, please see the Subcommittee's February 7, 2011, agenda.

Issue 1 – Budget Augmentation

Prior Subcommittee Action. At its February 7, 2011, hearing, the Subcommittee held this item open pending receipt of additional information.

Governor's Budget Request. The State Auditor requests an increase of $8.2 million ($4.7 million GF) and 34 positions in 2011-12 to fund a two-year plan to better assist the Legislature in its oversight of government operations, including conducting additional audits, completing more high risk analyses, and better integrating the audit process with the work of legislative budget and policy committees.

Background. Currently, the Auditor has 147 employees on staff. In Year 1 of this plan, the Auditor proposes to increase staffing by 34 positions, to a total of 181 positions. In Year 2, an additional 37 staff would be added, bringing staffing to a total of 218 positions. In Year 1, the Auditor reports that it will utilize $3.5 million of the requested funding to contract with outside experts to conduct the federal compliance audit work, thereby allowing the Auditor to utilize the remaining $4.5 million to recruit, hire, and train the 34 new in-house staff to conduct the additional mandated, discretionary, and high-risk audit work as well as investigations. These 34 staff will also respond to increases in other activities, such as inquiries and requests from legislative staff, legal assistance, and public record requests, due to the additional audits being completed. In Year 2, the Auditor reports that it should have a sufficient number of trained audit and investigative staff to conduct the increase in audit work and provide the additional integration with legislative oversight. Consequently, in Year 2, the Auditor plans to substantially reduce or eliminate the contracted federal compliance work to hire the additional 37 staff.

At the end of the two-year plan, which will result in the addition of 54 new audit staff, the Auditor reports that audit production will increase from the 2010-11 average of 30 audits per year, to 50-55 per year, including discretionary and mandated audits, as well as more work under the high-risk authority. The additional audit staff will also reduce the time it currently takes to complete an audit, and will also reduce staff burnout and a high turnover rate. The Auditor reports that the addition of eight investigative staff over the two years will result in self-initiated statewide investigations increasing from the 2010-11 average of one per year to four to eight per year.

The Auditor indicates that the additional audit and investigative results from the two-year plan will produce more monetary benefits for the state, and offers the following recent examples of savings from audit and investigative work: (1) $194 million in unallowable costs, plus $53 million in cost avoidance over seven years (State Mandates Audits, 2003 and 2009); (2) $3.3 million revenue increase (Citation Penalty Accounts, 2010-108); (3) $4.8 million in cost avoidance (Medi-Cal TARS, 2009-112); and (4) $12 million cost recovery (CalWorks, 2009-101).

0840 STATE CONTROLLER'S OFFICE (SCO)

For overview and budget information regarding this department, please see the Subcommittee's January 25, 2011, agenda.

Issue Proposed for Discussion / Vote:

Issue 1 – Unclaimed Property Legal Costs

Prior Subcommittee Action. This issue was held open at the Subcommittee's January 25, 2011, hearing pending receipt of additional information from the SCO.

Governor's Budget Request. The Governor requests a two-year augmentation of $300,000 (Unclaimed Property Fund) beginning in 2011-12 to provide representation in legal matters associated with representing the Unclaimed Property Program in lawsuits filed against the SCO.

Background. Under current law, the SCO is responsible for safeguarding unclaimed property until it is returned to its rightful owner. Claims processed through the Unclaimed Property Program are paid, returned for insufficient information, or denied. When a claim is denied, claimants are notified of their right to commence an action against the SCO pursuant to law. When these actions are taken, the SCO has 60 days to respond. In addition to these actions by individual claimants, other actions, including class action type suits in both state and federal court have been brought against the SCO. These suits allege the program is unconstitutional, claiming the SCO has not properly administered the program and is not seeking restitution for plaintiffs.

The Attorney General normally represents the SCO, but the SCO reports that the Attorney General does not have the resources to respond to all of the actions brought against the SCO. The SCO is requesting the additional funds for a limited amount of time to clear the existing lawsuits for only the most complex cases; the SCO views this as more cost effective than hiring permanent staff and training them for what may eventually result in a lack of workload. The SCO reports that it will be in a better position in two years to gauge the volume and complexity of lawsuits and perhaps the need for permanent staff, whether at the SCO or the Attorney General's Office.

Staff Comment. The resources in this request are to continue the use of outside counsel for two pre-existing class action lawsuits. Over the life of these lawsuits, the Attorney General's Office has approved the use of outside counsel. Staff concurs with the SCO's assessment that to change counsel midstream in these cases would not be prudent. Staff also notes that this request is a two-year limited-term increase in expenditure authority.

Staff Recommendation: Approve the budget request.

Vote: Budget request approved by a 2-1 vote; Senator La Malfa voting no.

1700 DEPARTMENT OF FAIR EMPLOYMENT AND HOUSING (DFEH)
1760 DEPARTMENT OF GENERAL SERVICES (DGS)

For overview and budget information regarding these departments, please see the Subcommittee's January 27, 2011, agenda.

Issue Proposed for Discussion / Vote:

Issue 1 – Information Technology Transfer to Department of General Services; Retain Two Positions for Enforcement

Prior Subcommittee Action. At its January 27, 2011, hearing, the Subcommittee: (1) approved the transfer of the DFEH IT function and workload to DGS; (2) swept the excess five positions at DGS as well as the $300,000 Service Revolving Fun; and (3) left open the DFEH requests to retain the two positions for enforcement and provide reimbursement to DGS for the transferred IT functions.

Governor's Budget Request. The Governor requests to permanently transfer DFEH's Information Technology (IT) function and five positions to the Department of General Services (DGS) and proposes budget provisional language that sets aside $507,000 GF from DFEH to pay for the transferred functions. In addition, the Governor proposes to redirect the two remaining IT positions to DFEH's enforcement division on a two-year limited-term basis to process claims resulting from the settlement of a class-action lawsuit.

Background. The DFEH entered into an agreement with the DGS effective July 2010 which transferred DFEH's entire IT function and five positions to DGS's IT unit and provided $465,000 to DGS for the cost of providing these services in 2010-11. One objective of this agreement was to achieve efficiency and cost savings.

In September 2010, DFEH reached its first multi-million dollar discrimination settlement, totaling more than $6.9 million. According to the DFEH, the settlement will result in a significant increase in workload. The DFEH, therefore, is proposing to retain the two remaining IT positions and convert them into two-year limited-term positions in its Special Investigations Unit to address expected new workload stemming from the settlement of 1,500 family leave claims. All claims are required to be submitted by February 15, 2011. Shortly thereafter, the designated third-party administrator will submit all timely and valid claim forms to DFEH and DFEH staff will then conduct an independent evaluation of each claim to determine whether, on a case-by-case basis, the claimant experienced a California Family Rights Act violation and, if so, the type of violation and the appropriate level of damages.

Staff Comment. When the Subcommittee initially considered this issue at its January 27, 2011, hearing, concerns were expressed that workload justifications had not been provided for: (1) DFEH to retain two positions for enforcement; and (2) DFEH to provide reimbursement to DGS for the cost of DGS providing IT functions to DFEH. These justifications are necessary; otherwise, the resources provided could be greater than is warranted.

Since that hearing, both DGS and DFEH have provided the requested workload justifications. With regard to the number of claims received under the class action lawsuit, DFEH is on track to receive the requisite number to justify the retention of the two positions on a two-year limited-term basis.

With regard to the transfer of DFEH's IT function to DGS, staff notes that this is the first time the DGS IT unit is taking on a transferred IT function under contract for another state department. Given that, staff recommends that this portion of the request also be made two-year limited-term to allow this transfer to be revisited and reexamined in two-year's time to determine if DFEH has seen a reduction in its costs by having DGS provide its IT function.

Staff Recommendation. Approve on a two-year limited-term basis the request for DFEH to: (1) retain two positions for enforcement activities and (2) provide reimbursement to DGS for the transferred IT function.

Vote: Staff recommendation approved by a 2-1 vote; Senator La Malfa voting no.

8860 DEPARTMENT OF FINANCE (DOF), CALIFORNIA RECOVERY TASK FORCE

For overview information regarding the California Recovery Task Force, please see the Subcommittee's January 27, 2011, agenda.

Issue Proposed for Discussion / Vote:

Issue 1 – California Recovery Task Force – ARRA Funds Oversight

Prior Subcommittee Action. This issue was held open at the Subcommittee's January 27, 2011, hearing pending receipt of additional information.

Governor's Budget Request. The Governor requests one-time funds totaling $1.6 million ($928,000 GF and $700,000 Central Service Cost Recovery Fund) to support oversight and reporting for remaining ARRA funds in 2011-12. In addition to supporting the California Recovery Task Force (CRTF), the resources in this request will also provide funding for the California Technology Agency (CaTA) and support staff at Department of Finance [Office of State Audits and Evaluations (OSAE) and Fiscal Systems Consulting Unit (FSCU)], providing information technology activities related to federally-required quarterly reports and continued audit support, respectively. Figure 1 below illustrates funding levels for the three entities comprising the CRTF generally:

Figure 1

	2010-11	**2011-12 Funding**
California Recovery Task Force	$1,700,000	$578,000
California Technology Agency	$1,400,000	$600,000
Department of Finance: (1) Office of State Audits and Evaluations; and, (2) Fiscal Systems Consulting Unit	$905,000	$450,000
TOTAL	**$4,005,000**	**$1,628,000**

**Note, the fund split is 57 percent GF and 43 percent Central Service Cost Recovery Fund.*

Background. The primary functions that remain in 2011-12 will be quarterly reporting, compliance monitoring, and ensuring that all deadlines related to retaining ARRA funds are met to avoid losing any money awarded due to failure to spend funds within the required timeframes or for other non-compliance issues. CRTF responsibilities diminish as funds are expended; therefore, this proposal significantly reduces the staffing of the CRTF to oversee the remaining ARRA funds and to provide continued quarterly reports. In September 2010, 1,121 ARRA grants remained; in 2011-12, that number will drop to 568 grants.

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Staff Comment. The proposed resources for the CRTF in 2011-12 have been reduced from the level provided in 2010-11 reflective of the declining workload. However, staff notes that this request proposes five positions for the CRTF itself and 4.9 borrowed staff from the Department of Finance. Staff finds that this level of staffing is still greater than needed to meet the reduced workload which now consists primarily of recipient reporting to the CAAT which is administered by the CaTA. Therefore, the Subcommittee may wish to further reduce the proposed staffing levels for the CRTF in 2011-12 by instead providing three positions for the CRTF itself to complete required ARRA workload and three borrowed positions from DOF to continue to provide a reduced audit/oversight role. Should the Subcommittee adopt this recommendation, the request would be decreased by $393,000 ($224,000 GF and $169,000 Central Service Cost Recovery Fund).

Staff Recommendation: Approve the request but reduce the 2011-12 resources for the California Recovery Task Force by $393,000 ($224,000 GF and $169,000 Central Service Cost Recovery Fund), including a reduction of two CRTF positions and $150,000 to reflect reduced OSAE support.

Vote: Staff recommendation approved by a 3-0 vote.

STATE OPERATIONS EFFICIENCIES

Governor's Budget Request. The January Governor's Budget includes $363 million ($200 million GF) in savings associated with identification of efficiencies in state operations; review of state peace officer and safety classifications; and reductions in other areas such as contracting, fleet operations, and cell phone use. The mechanism to achieve these savings is Control Section 3.91, which requires the Director of Finance to allocate the reductions necessary to each item of appropriation in the budget to accomplish the required savings.

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Issue Proposed for Discussion

Issue 1 - Fleet Management

Background. On January 28, 2011, Governor Brown issued an EO requiring that: (1) the state passenger car and truck fleet, comprised of approximately 11,000 non-public safety vehicles, be reduced by 50 percent; and (2) home storage permits, which currently total 4,500 (excluding public health and safety) and allow state employees to use passenger cars for their daily commute, be reduced by 50 percent. The EO requires that underutilized vehicles be moved to new locations, so that the state fleet will be more efficient overall, and requires all vehicles deemed "non-essential" be sold or transferred within 120 days of an approved analysis and plan for vehicle allocation/retention. The EO prohibits agencies and departments from buying new vehicles for non-emergency use. Finally, this EO supersedes the prior Administration's July 2009 EO on fleet management which required a reduction of the overall size of the fleet by at least 15 percent and a reduction of home vehicle storage permits by at least 20 percent.

Staff Comment. Presently, the Administration does not have a savings estimate attached to the EO. That information will likely become available after March 1, 2011, which is the date that departments and agencies are required to report into DOF the results of their internal review of their current fleet and home storage permits.

Committee Questions. Based on the above information, the Committee may wish the Administration to provide responses to the following questions:

1. How does this EO interact with the prior Administration's EO? Was that prior EO not fully implemented, so new reductions of 50 percent are achievable?
2. The state vehicle fleet is actually much larger than the 11,000 figure noted in the EO because public safety vehicles are excluded. Is the Administration certain that all of the vehicles used by public safety are in use and there no efficiencies to be gained?

Staff Recommendation. None; informational item only.

Issue Proposed for Discussion / Vote:

Issue 2 – Reduction in Department of General Services' Building Rental Rates

Governor's Request. The Governor requests uncodified trailer bill language to authorize the Director of Finance to reduce 2010-11 appropriations to reflect a reduction in the building rental rates charged to departments by the Department of General Services (DGS).

Background. DGS charges building rental rates for state owned buildings that fall into one of two categories: (1) Building Rental Account Buildings – no debt service; and (2) Individual Rate Buildings – with debt service. In both categories, the DGS charged rate is for costs to support and maintain the building, such as janitorial services and building maintenance. For buildings in the Individual Rate Building category, debt service costs are added to the cost to support and maintain the building.

The DGS has determined that its rental rates will decrease substantially in 2010-11 and 2011-12. More specifically, DGS has determined that the cost for Building Rental Account Buildings is decreasing from $1.80/square foot to $1.40/square foot in 2010-11 and to $1.12/square foot in 2011-12. The Individual Rate Buildings are also decreasing with varying costs depending on the building. Overall, the 2010-11 savings total an estimated $31.3 million and the 2011-12 savings total an estimated $27.5 million. DOF is continuing to work on an estimate of the fund splits (GF versus other funds); departmental input is necessary for a more precise estimate as DGS does not have that level of funding information.

Staff Comment. Generally speaking, the 40 cent decrease in the rate DGS is charging agencies and departments in 2010-11 is translating to reduced current year costs for those entities (and reduced levels of reimbursements for DGS). The decrease in 2010-11 is related to employee compensation savings, primarily from nine furlough days and the workforce cap which reduced personnel costs across all departments by five percent ongoing. The DOF reports that it can reduce most departmental budgets using the existing 2010 budget act authority contained in Control Section 3.90(b). However, there are a number of entities that are exempt from these provisions, many of which would have GF savings, including the courts, Franchise Tax Board, and Board of Equalization, as well as the constitutional officers. To capture the savings associated with these rate reductions, the Administration requests uncodified trailer bill language that authorizes the Director of Finance to reduce appropriations to reflect a reduction in the building rental rates charged to departments by DGS.

For 2011-12, the DOF has determined that Control Section 3.91, which relates to State Operations Efficiencies, provides the authority needed to capture these savings.

Staff concurs that additional authority is needed in the current year to ensure that all of these savings are captured.

Staff Recommendation. Approve trailer bill language to authorize the Administration to reduce appropriations in 2010-11 to reflect a reduction in building rental rates charged to departments by DGS.

Vote: Budget request approved by a 3-0 vote.

Senate Budget and Fiscal Review—Mark Leno, Chair

SUBCOMMITTEE NO. 4 Agenda

Senator Michael J. Rubio, Chair
Senator Noreen Evans
Senator Doug La Malfa

Thursday, February 10, 2011
9:30 a.m. or Upon Adjournment of Session
Room 112

Consultant: Seija Virtanen

PART C

Item Number and Title

1100	California Science Center
1110	Department of Consumer Affairs, Boards
1111	Department of Consumer Affairs, Bureaus
2400	Department of Managed Health Care

(See Table of Contents on page 2 for a More Specific Listing of Issues)

Pursuant to the Americans with Disabilities Act, individuals who, because of a disability, need special assistance to attend or participate in a Senate Committee hearing, or in connection with other Senate services, may request assistance at the Senate Rules Committee, 1020 N Street, Suite 255 or by calling 916-324-9335. Requests should be made one week in advance whenever possible.

AGENDA – VOTE ONLY ITEMS

(Please see summary chart on Page 3)

AGENDA – DISCUSSION / VOTE ITEMS

Issues Proposed for Vote Only:

	Issue	2011-12 Amount	Fund Source	Staff Recommendation
	Department of Consumer Affairs, Bureaus (1111)			
1	Bureau of Automotive Repair: Consumer Assistance Program Funding Realignment and Augmentation	$22.157 million and 12.3 PY; -$7.693 million and reduce 8 PY	Special Funds	APPROVE
	Department of Managed Health Care (2400)			
2	Health Care Reform	$1.4 million	Special Funds	APPROVE

Vote:

Issues Proposed for Vote Only – Issue Descriptions

DEPARTMENT OF CONSUMER AFFAIRS, BUREAUS (1111)

For overview and budget information regarding this department, please see page 8 of this agenda.

Issue 1 – Bureau of Automotive Repair: Consumer Assistance Program Funding Realignment and Augmentation

Bureau of Automotive Repair. The Bureau of Automotive Repair is responsible for regulating the automotive repair marketplace and administering the Smog Check Program. To carry out its mandate, the Bureau educates consumers, disciplines stations and technicians, seeks resolution to complaints, and licenses individuals and businesses. The Bureau also administers the nation's largest motor vehicle emissions reduction program.

Governor's Budget Request. The Governor requests $22.157 million and 12.3 positions from the Enhanced Fleet Modernization Subaccount in 2011-12 and ongoing. In addition, the Governor requests a reduction of $7.693 million and 8.0 positions from the High Polluter Repair or Removal Account.

Background. A key part of California's air quality emissions reduction strategy is to implement incentive-based air quality programs to encourage the early retirement and replacement of older vehicles with newer, cleaner ones. Older vehicles account for approximately 25 percent of the miles driven but contribute up to 75 percent of the emissions released. Reducing emissions from the older vehicles is a critical part of California's State Implementation Plan (SIP), which outlines the state's clean air strategy. The SIP is used by the federal government to determine the amount of federal transportation funds California will receive.

The Consumer Assistance Program (CAP) was started in 1997 and contains two parts: vehicle retirement and vehicle repair. Under the vehicle repair program, qualified low-income consumers can receive financial assistance of up to $500 to repair a vehicle that is unable to pass a biennial Smog Check inspection when it exceeds specified emission standards. To receive the repair assistance, eligible consumers must pay the initial $20 in repairs. Beginning in 2000, a directed vehicle repair program was started that allowed qualified consumers who owned a vehicle directed to a Test-Only or Gold Shield Smog Check station for an initial inspection to receive up to $500 in additional financial assistance toward emissions-related repairs after they paid the first $100 of repairs. Directed vehicles are identified by the Bureau of Automotive Repair.

Under the vehicle retirement program, until August 2010, consumers were paid $1,000 to retire a vehicle. These funds are not paid until after the vehicle is dismantled.

The passage of AB 787 (Hill, 2010) makes several additional changes to CAP. Under AB 787 the Bureau of Automotive Repair must offer all eligible low-income consumers an additional $500 to retire a vehicle through CAP. AB 787 also allows any vehicle that has been registered in California for two continuous years and has failed a lawfully required Smog Check inspection to be retired through CAP.

AB 787 also eliminates the provision of law authorizing owners of directed vehicles the ability to participate in the repair assistance option of CAP based solely on this designation and receive $500 toward emissions-related repairs.

DEPARTMENT OF MANAGED HEALTH CARE (2400)

For overview and budget information regarding this department, please see page 11 of this agenda.

Issue 2 – Health Care Reform

Governor's Budget Request. The Governor requests $1,776,000 for 13.0 two-year limited-term positions to address new workload resulting from the March 2010 federal Health Care Reform Legislation.

Background. On March 23, 2010, President Obama signed into law comprehensive health care reform, the Patient Protection and Affordable Care Act, which was subsequently modified by the Health Care and Education Reconciliation Act of 2010 (hereinafter referred to as "Health Care Reform"). Health Care Reform will fundamentally alter the availability and structure of health insurance, bring coverage for the first time to millions of Californians, and bring new coverage options for millions of enrollees who receive care through California Knox-Keene Licensed health plans and contracted medical groups.

In light of the recent enactment of Health Care Reform, DMHC must take immediate action to assess and address the impacts of the reform on its mission critical operations. In response to Health Care Reform, DMHC will have to develop state regulations, review health plan documentation to comply with the new law, and respond to consumer inquiries.

The Department of Managed Health Care (DMHC) has explained that the positions are requested on a two-year limited-term basis not because DMHC expects the workload to be temporary, but to monitor the activity that results from Health Care Reform to determine if the workload assumptions hold true. Over the course of the two years, once all impacts are considered and a better assessment of new Health Care Reform workload results, the department will submit a future Budget Change Proposal to address the new permanent workload generated by the Health Care Reform legislation.

1100 CALIFORNIA SCIENCE CENTER

Department Overview. The California Science Center is an educational, scientific, and technological center located in Exposition Park, a 160-acre tract in south Los Angeles. The Science Center has interactive exhibits on human inventions and innovations, the life processes of living things, and temporary exhibits. The California African American Museum (CAAM), also included in the park, provides exhibitions and programs on the history, art, and culture of African Americans. In addition, the Office of the Park Manager is responsible for maintenance of the park, public safety, and parking facilities.

Budget Overview. The January Governor's Budget provides 190 authorized positions and $28.1 million ($19.4 million GF). It should be noted that the California Science Center budget includes the California African American Museum, Exposition Park Management, and facilities bond repayments. The reduction to the Science Center's operations is $3.66 million General Fund.

Issues Proposed for Discussion / Vote

Issue 1 – Unallocated Budget Reduction

Governor's Budget Request. The Governor requests an unallocated reduction of $3,660,000 to the Science Center's budget. The Governor also requests budget bill language to allow the Science Center to collect an admissions fee.

Background. The unallocated reduction of $3.7 million is 20 percent of the amount of General Fund remaining after excluding amounts budgeted for lease-revenue payments ($4.8 million). The General Fund base used for the calculation is $18.3 million ($23.1 million total General Fund less the $4.8 million).

The Science Center's operations have been based on the value that everyone is allowed access, and thus no admission fee has been charged. The Science Center does charge for parking and the IMAX movie tickets.

Staff Comment. Approximately one-third of the Science Center's visitors are school groups, which would be unlikely to afford admissions fees for each student, due to the funding restrictions that local school districts are currently experiencing.

Staff thinks that there are some possibilities for the Science Center to raise revenue that does not compromise the Science Center's dedication to free admission. The Science Center already charges $8 for parking, and $25 for parking at special events. (The Science Center also charges for their IMAX movie tickets.) It may be possible to raise additional revenue through increasing the parking fee from $8 to $10. The increase in parking fees would also apply to events at Exposition Park, including football games and concerts. Based on past Science Center parking fee increase revenue collections, staff estimates that the Science Center can collect approximately $800,000 in new revenue from raising parking fees.

The Office of the Exposition Park Management has an executive director appointed by the Governor for the purpose of managing, scheduling, and administering all park related events, including oversight for the police and security services of the park.

Staff Recommendation: Staff recommends the following:

1. Reject the Governor's budget request.
2. Reject item 1100-001-0001 Provisional Language 1 and 2.
3. Approve a $1.7 million unallocated reduction to the Science Center.
4. Approve an increase of $850,000 in expenditure authority to the Exposition Park Improvement Fund (0267).
5. Approve budget bill language that specifies that the California African American Museum not be reduced by more than $95,000.
6. Approve budget bill language stating legislative intent that parking rate increases are preferred to general admission charges at either the California Science Center or the California African American Museum.
7. Approve trailer bill language for the elimination of the Office of Exposition Park Management and return those functions to the Science Center.
8. Approve trailer bill language authorizing non-civil service staff to perform facility support services at the Science Center.

Vote:

1110/1111 DEPARTMENT OF CONSUMER AFFAIRS

Departmental Overview and Mission. The Department of Consumer Affair's (DCA) Boards and Bureaus provide exams and licensing, enforcement, complaint mediation, education for consumers, and information on privacy concerns. DCA Boards and Bureaus establish minimal competency standards for more than 255 professions involving approximately 2.4 million professionals. There are currently 25 boards, a commission, three committees, and eight bureaus under the broad authority of the DCA.

Budget Overview. The Boards are budgeted under organizational code 1110, and the total proposed budget is $271.46 million (no General Fund) and 1,511.3 positions – an increase of $10.4 million and 35.6 positions over 2010-11.

The Bureaus are budgeted under organizational code 1111, and the total proposed budget is $231.34 million (no General Fund) and 1,386.6 positions – an increase of $14.2 million and 5.7 positions over 2010-11.

DCA Boards and Bureaus

(dollars in thousands)

		Positions		Expenditures	
		2010-11	2011-12	2010-11	2011-12
1	Board of Accountancy	82.5	85.8	$ 12,210	$ 11,452
2	Architects Board	30.1	30.1	$ 4,686	$ 4,760
3	Athletic Commission	13.7	13.7	$ 2,541	$ 2,613
4	Board of Behavioral Science	42.6	43.4	$ 8,090	$ 7,898
5	Barbering and Cosmetology	95.1	95.1	$ 17,303	$ 18,291
6	Contractors State Licensing	402.1	402.1	$ 57,514	$ 59,979
7	Dental Board	71.6	75.1	$ 12,652	$ 13,496
8	Dental Hygiene Committee	6.2	6.7	$ 1,242	$ 1,358
9	Guide Dogs for the Blind	1.5	1.5	$ 180	$ 187
10	Medical Board	265.5	276.7	$ 52,385	$ 55,843
11	Acupuncture Board	7.9	8.0	$ 2,548	$ 2,603
12	Physical Theraphy Board	15.0	16.4	$ 2,910	$ 3,290
13	Physician Assistant Com.	4.7	4.8	$ 1,387	$ 1,418
14	Podiatric Medicine	4.6	4.6	$ 1,362	$ 1,381
15	Psychology	15.3	18.3	$ 3,879	$ 4,335
16	Respiratory Care Board	15.9	16.1	$ 3,035	$ 3,138
17	Speech-Language Pathology	8.1	8.2	$ 1,848	$ 1,615
18	Occupational Therapy	10.5	10.2	$ 1,417	$ 1,473
19	Board of Optometry	10.9	11.1	$ 1,654	$ 1,574
20	Osteopathic Medical Board	10.6	11.7	$ 1,916	$ 2,045
21	Naturopathic Medicine Com.	0.9	0.9	$ 130	$ 141
22	Board of Pharmacy	75.4	80.0	$ 13,021	$ 14,448
23	Engineers and Land Surveyors	65.6	65.6	$ 10,397	$ 10,774
24	Registered Nursing	128.0	135.6	$ 28,250	$ 29,242
25	Court Reporters Board	4.3	4.3	$ 1,096	$ 1,114
26	Veterinary Medical Board	12.4	12.0	$ 2,639	$ 2,757
27	Vocational Nursing	74.7	73.3	$ 14,743	$ 14,237
28	Arbitration Certification Prog.	7.6	7.6	$ 1,098	$ 1,107
29	Security and Investigative	50.2	50.7	$ 11,363	$ 11,865
30	Private Postsecondary Ed.	55.8	55.8	$ 10,160	$ 9,368
31	Electronic and Appliance Repair, Home Furnishings, and Thermal Insulation	41.9	41.9	$ 7,108	$ 7,781
32	Automotive Repair	596.2	600.2	$ 182,192	$ 195,798
33	Telephone Medical Advise Services Bureau	0.9	0.9	$ 145	$ 148
34	Cemetery and Funeral	21.2	18.5	$ 4,006	$ 4,149
35	Professional Fiduciaries	1.6	1.6	$ 282	$ 308

Issue Proposed for Discussion / Vote:

Issue 1 – Board of Accountancy and Dental Board: Loan Repayment

Dental Board of California. The Dental Board of California establishes minimal standards of competency for those individuals seeking to practice as a dentist, registered dental hygienist, registered dental assistant, dental auxiliary in extended function, or dental hygienist in alternative practice. The Board enforces standards to protect California dental consumers from incompetent dental practitioners, and the utilization of dental auxiliaries contributes to providing quality dental services to Californians.

Effective January 1, 2009, the State Dental Assistant Committee (Committee) was created and assumed the duties of the Committee on Dental Auxiliaries with regard to dental assistants, pursuant to Chapter 31, Statutes of 2008 (SB 853).

Governor's Budget Request. The Governor requests repayment of two loans from the General Fund to special funds: 1) $10 million repayment by the General Fund to the Accountancy Fund, and 2) $2.5 million repayment by the General Fund to the State Dentistry Fund.

Background. During the 2010-11 fiscal year, the State loaned $10 million from the Accountancy Fund to the General Fund. This amount is set to be repaid in June 2012.

During the 2002-03 fiscal year, the State loaned $2.5 million from the State Dentistry Fund to the General Fund. This amount is set to be repaid in June 2012.

Staff Comment. The Accountancy Fund loan repayment can be delayed by one year without having an influence on the Board's programs.

$1.3 million of the loan from the State Dentistry Fund can be delayed by one year without having an influence on the Board's programs.

Staff Recommendation. Delay repayment of the Accountancy Fund $10 million loan until June 30, 2013. Include the following budget bill language:

Add Item 1110-404:
1110-404—Notwithstanding Provision 1 of Item 1110-011-0704, Budget Act of 2010 (Ch. 712, Stats. 2010), the $10,000,000 loan to the General Fund will be repaid in fiscal year 2012-13 upon order of the Director of Finance.

Delay repayment of $1.3 million of the State Dentistry Fund loan repayment until June 30, 2013. Include the following budget bill language:

Add Item 1110-405:
1110-405—Notwithstanding Provision 1 of Item 1250-011-0741, Budget Act of 2003 (Ch. 157, Stats. 2003), the $1,300,000 loan to the General Fund will be repaid in fiscal year 2012-13 upon order of the Director of Finance.

Vote:

2400 DEPARTMENT OF MANAGED HEALTH CARE

Department Overview. The Department of Managed Health Care (DMHC) was established in 2000, when the licensure and regulation of the managed health care industry was removed from the Department of Corporations and placed in a new, stand-alone, department. The mission of DMHC is to regulate, and provide quality-of-care and fiscal oversight for Health Maintenance Organizations (HMOs) and two Preferred Provider Organizations (PPOs). These 94 Health Care Plans provide health insurance coverage to approximately 64 percent of all Californians. Recent statutory changes also make DMHC responsible for the oversight of 240 Risk Bearing Organizations (RBOs), who actually deliver or manage a large proportion of the health care services provided to consumers. Within the Department, the Office of the Patient Advocate helps educate consumers about their HMO rights and responsibilities.

Budget Overview. The January Governor's Budget provides DFI with 250.2 authorized positions and $35 million (no GF). This is an increase of 2.7 positions and $55,000 over 2010-11.

Issues Proposed for Discussion / Vote:

Issue 1 – Senate Bill 1163 Premium Rate Review

Governor's Budget Request. The Governor requests 2.0 positions and $1,024,000 from the Managed Care Fund for FY 2011-12 and $908,000 for FY 2012-13 and ongoing (from the Managed Care Fund) to address new workload attributable to health plan rate increase review as specified in the federal Patient Protection and Affordable Care Act (PPACA or Health Care Reform) signed into law on March 23, 2010 and supported by Senate Bill 1163 enacted on September 30, 2010. Of the funds requested, $100,000 is one-time for an information technology consultant to assist with website design in accordance with public information disclosure requirements, and $600,000 is on-going for an external contract with an actuarial consultant.

Background. The Legislature passed, and the Governor signed, SB 1163 (Leno, 2010) to begin aligning California's laws with the federal Health Care Reform Act. With the passage of SB 1163, many of DMHC's roles and responsibilities for implementing Health Care Reform are defined and DMHC has been provided the authority to enforce the federal mandates in the state of California.

SB 1163 requires insurers to file rate information with DMHC that has been verified by an independent actuary under contract to the insurer. DMHC must make the rate information publicly available and verify rate information when it appears that a company may have violated the rate review process. DMHC must also provide information to the California Health Benefits Exchange and fulfill certain federal and state reporting requirements for health insurance rates.

Staff Comment. The workload associated with SB 1163 is new and thus there is uncertainty about the number of hours that will need to be devoted to the tasks DMHC is

required to undertake. Thus, staff thinks the requested positions should be made limited-term so that workload can be revisited in two years.

The funds for an external consultant to conduct actuarial review should be made limited-term (two-year) because it is not known what will be the actual workload. Also, DMHC should consider ways of bringing the actuarial review in-house rather than having a consultant contract indefinitely.

Staff Recommendation: Approve funds for two years and positions as two-year limited-term. Also, approve supplemental reporting language to have DMHC submit a report considering options for bringing actuarial review in-house.

Vote:

Senate Budget and Fiscal Review—Mark Leno, Chair

SUBCOMMITTEE NO. 4 Outcomes

Senator Michael J. Rubio, Chair
Senator Noreen Evans
Senator Doug La Malfa

Thursday, February 10, 2011

Consultant: Seija Virtanen

PART C

Item Number and Title

1100	California Science Center
1110	Department of Consumer Affairs, Boards
1111	Department of Consumer Affairs, Bureaus
2400	Department of Managed Health Care

(See Table of Contents on page 2 for a More Specific Listing of Issues)

AGENDA – VOTE ONLY ITEMS

(Please see summary chart on Page 3)

AGENDA – DISCUSSION / VOTE ITEMS

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	Department of Managed Health Care (2400)			
2	Health Care Reform	$1.4 million	Special Funds	APPROVE

Vote: **2-1 (La Malfa voted no)**

DEPARTMENT OF CONSUMER AFFAIRS, BUREAUS (1111)

For overview and budget information regarding this department, please see page 8 of this agenda.

Issue 1 – Bureau of Automotive Repair: Consumer Assistance Program Funding Realignment and Augmentation

Bureau of Automotive Repair. The Bureau of Automotive Repair is responsible for regulating the automotive repair marketplace and administering the Smog Check Program. To carry out its mandate, the Bureau educates consumers, disciplines stations and technicians, seeks resolution to complaints, and licenses individuals and businesses. The Bureau also administers the nation's largest motor vehicle emissions reduction program.

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DEPARTMENT OF MANAGED HEALTH CARE (2400)

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Issue 2 – Health Care Reform

Governor's Budget Request. The Governor requests $1,776,000 for 13.0 two-year limited-term positions to address new workload resulting from the March 2010 federal Health Care Reform Legislation.

Background. On March 23, 2010, President Obama signed into law comprehensive health care reform, the Patient Protection and Affordable Care Act, which was subsequently modified by the Health Care and Education Reconciliation Act of 2010 (hereinafter referred to as "Health Care Reform"). Health Care Reform will fundamentally alter the availability and structure of health insurance, bring coverage for the first time to millions of Californians, and bring new coverage options for millions of enrollees who receive care through California Knox-Keene Licensed health plans and contracted medical groups.

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1100 CALIFORNIA SCIENCE CENTER

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Issues Proposed for Discussion / Vote

Issue 1 – Unallocated Budget Reduction

Governor's Budget Request. The Governor requests an unallocated reduction of $3,660,000 to the Science Center's budget. The Governor also requests budget bill language to allow the Science Center to collect an admissions fee.

Background. The unallocated reduction of $3.7 million is 20 percent of the amount of General Fund remaining after excluding amounts budgeted for lease-revenue payments ($4.8 million). The General Fund base used for the calculation is $18.3 million ($23.1 million total General Fund less the $4.8 million).

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Staff Recommendation: Staff recommends the following:

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2. Reject item 1100-001-0001 Provisional Language 1 and 2.
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6. Approve budget bill language stating legislative intent that parking rate increases are preferred to general admission charges at either the California Science Center or the California African American Museum.
7. Approve trailer bill language for the elimination of the Office of Exposition Park Management and return those functions to the Science Center.
8. Approve trailer bill language authorizing non-civil service staff to perform facility support services at the Science Center.

Vote: **Action taken was approval of staff recommendation items 1, 2, 3, 4, 5, 6, and 7; and rejection of staff recommendation 8.**

2-1 (La Malfa voted no)

1110/1111 DEPARTMENT OF CONSUMER AFFAIRS

Departmental Overview and Mission. The Department of Consumer Affair's (DCA) Boards and Bureaus provide exams and licensing, enforcement, complaint mediation, education for consumers, and information on privacy concerns. DCA Boards and Bureaus establish minimal competency standards for more than 255 professions involving approximately 2.4 million professionals. There are currently 25 boards, a commission, three committees, and eight bureaus under the broad authority of the DCA.

Budget Overview. The Boards are budgeted under organizational code 1110, and the total proposed budget is $271.46 million (no General Fund) and 1,511.3 positions – an increase of $10.4 million and 35.6 positions over 2010-11.

The Bureaus are budgeted under organizational code 1111, and the total proposed budget is $231.34 million (no General Fund) and 1,386.6 positions – an increase of $14.2 million and 5.7 positions over 2010-11.

DCA Boards and Bureaus

(dollars in thousands)

		Positions		Expenditures	
		2010-11	2011-12	2010-11	2011-12
1	Board of Accountancy	82.5	85.8	$ 12,210	$ 11,452
2	Architects Board	30.1	30.1	$ 4,686	$ 4,760
3	Athletic Commission	13.7	13.7	$ 2,541	$ 2,613
4	Board of Behavioral Science	42.6	43.4	$ 8,090	$ 7,898
5	Barbering and Cosmetology	95.1	95.1	$ 17,303	$ 18,291
6	Contractors State Licensing	402.1	402.1	$ 57,514	$ 59,979
7	Dental Board	71.6	75.1	$ 12,652	$ 13,496
8	Dental Hygiene Committee	6.2	6.7	$ 1,242	$ 1,358
9	Guide Dogs for the Blind	1.5	1.5	$ 180	$ 187
10	Medical Board	265.5	276.7	$ 52,385	$ 55,843
11	Acupuncture Board	7.9	8.0	$ 2,548	$ 2,603
12	Physical Theraphy Board	15.0	16.4	$ 2,910	$ 3,290
13	Physician Assistant Com.	4.7	4.8	$ 1,387	$ 1,418
14	Podiatric Medicine	4.6	4.6	$ 1,362	$ 1,381
15	Psychology	15.3	18.3	$ 3,879	$ 4,335
16	Respiratory Care Board	15.9	16.1	$ 3,035	$ 3,138
17	Speech-Language Pathology	8.1	8.2	$ 1,848	$ 1,615
18	Occupational Therapy	10.5	10.2	$ 1,417	$ 1,473
19	Board of Optometry	10.9	11.1	$ 1,654	$ 1,574
20	Osteopathic Medical Board	10.6	11.7	$ 1,916	$ 2,045
21	Naturopathic Medicine Com.	0.9	0.9	$ 130	$ 141
22	Board of Pharmacy	75.4	80.0	$ 13,021	$ 14,448
23	Engineers and Land Surveyors	65.6	65.6	$ 10,397	$ 10,774
24	Registered Nursing	128.0	135.6	$ 28,250	$ 29,242
25	Court Reporters Board	4.3	4.3	$ 1,096	$ 1,114
26	Veterinary Medical Board	12.4	12.0	$ 2,639	$ 2,757
27	Vocational Nursing	74.7	73.3	$ 14,743	$ 14,237
28	Arbitration Certification Prog.	7.6	7.6	$ 1,098	$ 1,107
29	Security and Investigative	50.2	50.7	$ 11,363	$ 11,865
30	Private Postsecondary Ed.	55.8	55.8	$ 10,160	$ 9,368
31	Electronic and Appliance Repair, Home Furnishings, and Thermal Insulation	41.9	41.9	$ 7,108	$ 7,781
32	Automotive Repair	596.2	600.2	$ 182,192	$ 195,798
33	Telephone Medical Advise Services Bureau	0.9	0.9	$ 145	$ 148
34	Cemetery and Funeral	21.2	18.5	$ 4,006	$ 4,149
35	Professional Fiduciaries	1.6	1.6	$ 282	$ 308

Issue Proposed for Discussion / Vote:

Issue 1 – Board of Accountancy and Dental Board: Loan Repayment

Dental Board of California. The Dental Board of California establishes minimal standards of competency for those individuals seeking to practice as a dentist, registered dental hygienist, registered dental assistant, dental auxiliary in extended function, or dental hygienist in alternative practice. The Board enforces standards to protect California dental consumers from incompetent dental practitioners, and the utilization of dental auxiliaries contributes to providing quality dental services to Californians.

Effective January 1, 2009, the State Dental Assistant Committee (Committee) was created and assumed the duties of the Committee on Dental Auxiliaries with regard to dental assistants, pursuant to Chapter 31, Statutes of 2008 (SB 853).

Governor's Budget Request. The Governor requests repayment of two loans from the General Fund to special funds: 1) $10 million repayment by the General Fund to the Accountancy Fund, and 2) $2.5 million repayment by the General Fund to the State Dentistry Fund.

Background. During the 2010-11 fiscal year, the State loaned $10 million from the Accountancy Fund to the General Fund. This amount is set to be repaid in June 2012.

During the 2002-03 fiscal year, the State loaned $2.5 million from the State Dentistry Fund to the General Fund. This amount is set to be repaid in June 2012.

Staff Comment. The Accountancy Fund loan repayment can be delayed by one year without having an influence on the Board's programs.

$1.3 million of the loan from the State Dentistry Fund can be delayed by one year without having an influence on the Board's programs.

Staff Recommendation. Delay repayment of the Accountancy Fund $10 million loan until June 30, 2013. Include the following budget bill language:

Add Item 1110-404:
1110-404—Notwithstanding Provision 1 of Item 1110-011-0704, Budget Act of 2010 (Ch. 712, Stats. 2010), the $10,000,000 loan to the General Fund will be repaid in fiscal year 2012-13 upon order of the Director of Finance.

Delay repayment of $1.3 million of the State Dentistry Fund loan repayment until June 30, 2013. Include the following budget bill language:

Add Item 1110-405:
1110-405—Notwithstanding Provision 1 of Item 1250-011-0741, Budget Act of 2003 (Ch. 157, Stats. 2003), the $1,300,000 loan to the General Fund will be repaid in fiscal year 2012-13 upon order of the Director of Finance.

Vote: **2-1 (La Malfa voted no)**

2400 DEPARTMENT OF MANAGED HEALTH CARE

Department Overview. The Department of Managed Health Care (DMHC) was established in 2000, when the licensure and regulation of the managed health care industry was removed from the Department of Corporations and placed in a new, stand-alone, department. The mission of DMHC is to regulate, and provide quality-of-care and fiscal oversight for Health Maintenance Organizations (HMOs) and two Preferred Provider Organizations (PPOs). These 94 Health Care Plans provide health insurance coverage to approximately 64 percent of all Californians. Recent statutory changes also make DMHC responsible for the oversight of 240 Risk Bearing Organizations (RBOs), who actually deliver or manage a large proportion of the health care services provided to consumers. Within the Department, the Office of the Patient Advocate helps educate consumers about their HMO rights and responsibilities.

Budget Overview. The January Governor's Budget provides DFI with 250.2 authorized positions and $35 million (no GF). This is an increase of 2.7 positions and $55,000 over 2010-11.

Issues Proposed for Discussion / Vote:

Issue 1 – Senate Bill 1163 Premium Rate Review

Governor's Budget Request. The Governor requests 2.0 positions and $1,024,000 from the Managed Care Fund for FY 2011-12 and $908,000 for FY 2012-13 and ongoing (from the Managed Care Fund) to address new workload attributable to health plan rate increase review as specified in the federal Patient Protection and Affordable Care Act (PPACA or Health Care Reform) signed into law on March 23, 2010 and supported by Senate Bill 1163 enacted on September 30, 2010. Of the funds requested, $100,000 is one-time for an information technology consultant to assist with website design in accordance with public information disclosure requirements, and $600,000 is on-going for an external contract with an actuarial consultant.

Background. The Legislature passed, and the Governor signed, SB 1163 (Leno, 2010) to begin aligning California's laws with the federal Health Care Reform Act. With the passage of SB 1163, many of DMHC's roles and responsibilities for implementing Health Care Reform are defined and DMHC has been provided the authority to enforce the federal mandates in the state of California.

SB 1163 requires insurers to file rate information with DMHC that has been verified by an independent actuary under contract to the insurer. DMHC must make the rate information publicly available and verify rate information when it appears that a company may have violated the rate review process. DMHC must also provide information to the California Health Benefits Exchange and fulfill certain federal and state reporting requirements for health insurance rates.

Staff Comment. The workload associated with SB 1163 is new and thus there is uncertainty about the number of hours that will need to be devoted to the tasks DMHC is

required to undertake. Thus, staff thinks the requested positions should be made limited-term so that workload can be revisited in two years.

The funds for an external consultant to conduct actuarial review should be made limited-term (two-year) because it is not known what will be the actual workload. Also, DMHC should consider ways of bringing the actuarial review in-house rather than having a consultant contract indefinitely.

Staff Recommendation: Approve funds for two years and positions as two-year limited-term. Also, approve supplemental reporting language to have DMHC submit a report considering options for bringing actuarial review in-house.

Vote: **Approved funds for two years and positions as two-year limited-term positions. Also, approved supplemental reporting language to have DMHC submit a report considering options for bringing actuarial review in-house.**

2-1 (La Malfa voted no)

Senate Budget and Fiscal Review—Mark Leno, Chair

SUBCOMMITTEE NO. 4 Agenda

Senator Michael J. Rubio, Chair
Senator Noreen Evans
Senator Doug LaMalfa

Thursday, May 5, 2011
9:30 a.m. or Upon Adjournment of Session
Room 112

Consultants: Brian Annis, Keely Bosler,
Kris Kuzmich, and Seija Virtanen

JANUARY BUDGET REQUESTS DENIED WITHOUT PREJUDICE AND APRIL FINANCE LETTERS

DEPARTMENTS TO BE HEARD

(Please See Detailed Agenda on Pages 2 and 3 for More Specific Listing and Order of Departments and Issues to Be Heard)

0502	California Technology Agency
0520	Secretary of Business, Transportation, and Housing Agency
0840	State Controller's Office
0845	Department of Insurance
0890	Secretary of State's Office
0971	California Alternative Energy and Advanced Transportation Authority
1110	Department of Consumer Affairs
1730	Franchise Tax Board
2320	Department of Real Estate
8380	Department of Personnel Administration
8880	Financial Information System for California (FI$Cal)
8955	California Department of Veterans Affairs

AGENDA – VOTE ONLY ITEMS

(Please see summary chart on Page 4)

AGENDA – DISCUSSION / VOTE ITEMS

Issues Proposed for Vote Only:

	Issue	Amount	Fund Source	Staff Recommendation
	Secretary of Business Transportation and Housing Agency (0520)			
1	Small Business Loan Guarantee Program Expansion	$84.4 million scheduled over three fiscal years.	Federal Funds	APPROVE, as specified
	State Controller's Office (0840)			
1	Increased Postage Expenses	$43,000 in 2010-11 $217,000 in 2011-12 and ongoing	Reimbursements	APPROVE
2	Transportation Audits Indirect Allocation Plans	$1,751,000 in 2011-12 and 12.6 two-year limited-term positions (Includes supplemental reporting language)	Reimbursements	APPROVE, as specified
	Department of Insurance (0845)			
1	Workers' Compensation Insurance Fraud Program: Local Assistance Workload Increases	$1,646,000 in 2011-12	Insurance Fund	APPROVE
	California Alternative Energy and Advanced Transportation Authority (0971)			
1	Energy Upgrade California Program	$205,000 in 2011-12	Reimbursements	APPROVE
	Department of Consumer Affairs (1110)			
1	Board of Professional Engineers and Land Surveyors Licensing Exams	$1,124,000 on a one-time basis	Special Funds	APPROVE
	Franchise Tax Board (1730)			
1	Data Security and Reliability: Enterprise Tape Library	Shift $2,290,000 from 2010-11 to 2011-12	General Fund	APPROVE
2	Voluntary Contribution Funding Codes: Budget Bill Clean-up	Language only	Language only	APPROVE
	Department of Real Estate (2320)			
1	SB 36 Mortgage Loan Originator Licensure (SAFE Act)	$216,000 in 2011-12 and 2 positions	Real Estate Fund	DENY
	Department of Personnel Administration (8380)			
1	Removal of Recruitment Contract Funding and Language	$350,000 in 2011-12 and modified budget bill language $350,000 in 2010-11 $350,000 in 2009-10	General Fund	APPROVE, as specified

Vote:

Issues Proposed for Vote Only – Issue Descriptions

SECRETARY OF BUSINESS, TRANSPORTATION, AND HOUSING AGENCY (0520)

Department Overview: The Secretary of the Business, Transportation and Housing Agency (BT&H Agency) is a member of the Governor's Cabinet and oversees 16 departments, including the following large departments:

- Alcoholic Beverage Control
- Corporations
- Housing and Community Development
- California Highway Patrol
- Motor Vehicles
- Financial Institutions
- Real Estate
- Managed Health Care
- Transportation

In addition, the Secretary's Office oversees programs, including the following, which are budgeted directly in the Secretary's Office:

- Infrastructure and Economic Development Bank
- Film Commission
- Small Business Loan Guarantee Program
- Tourism Commission

Budget Overview: The January Governor's Budget proposed total expenditures of $100.9 million ($4.2 million General Fund) and 60.7 positions for the Office of the Secretary – an increase of $78.2 million from the adjusted 2010-11 budget, and an increase of 1.5 funded positions. The primary reason for the year-over-year change is a one-time federal grant of $84.4 million to support the Small Business Loan Guarantee Program.

Current Budget Status: The Legislature made some modifications to the proposed budget for the Small Business Loan Guarantee Program, but otherwise approved the BT&H Agency budget as proposed. An April 1 Finance Letter was proposed to make some technical scheduling adjustments for federal grants to the Small Business Loan Guarantee Program which is discussed below as Issue 1.

Issue 1 –Small Business Loan Guarantee Program Expansion

April Letter Request. The Governor's April 1st Letter adjusts the budget to correctly reflect federal funds by year of receipt for the grants awarded to the Small Business Loan Guarantee Program. Instead of $84.4 million being received in 2011-12 (as was scheduled in the January Budget), the funds would be received as follows: $27.8 million in 2010-11, $27.8 million in 2011-12, and $28.7 million in 2012-13.

Background. The Governor's Budget requested various budget changes related to a federal grant award that will result in a one-time federal grant of $84.4 million for the Small Business Loan Guarantee Program (SBLG). This represents a significant expansion of the program which has typically had a trust-fund balance between $30 million and $40 million. The SBLG Program provides assistance to small businesses that may not qualify for traditional loans, by guaranteeing a portion of the loaned amount. The Administration requests to revert $20 million in General Fund support provided to the program one-time as part of the 2010 Budget Act (AB 1632, Chapter 731, Statutes of 2010). This reversion of $20 million is contingent on receipt of the federal funds. Finally, the Administration requests to double program staff from 1.5 positions to 3.0 positions.

Prior Subcommittee Action. The Subcommittee heard this item February 3 and February 10 and determined that the Federal grant will allow the State to expand this program, and at the same time realize a GF benefit of $20 million by reverting the augmentation provided last year. Specifically, the Subcommittee adopted the following:

a) The Governor's proposal to revert $20 million to the GF;
b) Budget Trailer Bill Language to direct that new loan guarantees use federal funds first;
c) Approved 0.5 new staff instead of 1.5 new staff;
d) Converted program administration funding to 50-percent GF and trust fund interest, and 50-percent federal funds, instead of eliminating all GF support for administration. This provided additional FDC administration funding over the base level for ramp-up, but still resulted in a GF expenditure savings; and,
e) Adopted provisional budget bill language to allow the Director of Finance to transfer up to $20 million from the GF to the Trust Fund, if loan defaults reduce the trust fund balance to the extent additional funds are necessary to maintain a 5:1 reserve ratio for outstanding loans. Joint Legislative Budget Committee (JLBC) notification would be required.

Staff Comment: To correctly reflect the installment appropriation for the $84.4 million grant, the Joint Legislative Budget Committee approved $27.8 million in federal expenditure authority for the Small Business Loan Guarantee Program in 2010-11 on March 25, 2011. The 30-day review period was waived so that the program would be positioned to meet the federal government's expectations for use of these funds.

The April 1st Letter proposes budget changes to correctly reflect the multi-year payment of the federal grant. The language would place $27.8 million into the Small Business Expansion Fund (consistent with federal regulations) for 2011-12.

This is recommended as vote-only because this is a technical fix, to correctly schedule the federal grant by fiscal year – there are no substantive changes to the proposal.

Staff Recommendation: Adopt the Administration's April 1st scheduling of federal funds, but maintain prior Subcommittee Action related to administrative costs and budget language.

STATE CONTROLLER'S OFFICE (0840)

For overview and budget information regarding the State Controller's Office (SCO), please see page 33 of this agenda.

Issue 1 – Increased Postage Expenses

April Letter Request. In an April Finance Letter, the Governor requests increased expenditure authority of $43,000 (reimbursements) in 2010-11 and $217,000 (reimbursements) in 2011-12 and ongoing, for increased postage expenses.

Background. The SCO is the chief financial officer of the state, whose responsibilities include mission critical functions such as general disbursements of payments and other mailings, which require postage. The cost of postage represents approximately 27 percent of the SCO's total ongoing 2011-12 Operating Expenses and Equipment budget. Actual postage costs for 2009-10 were $13 million and are budgeted at $14.2 million for 2010-11. As a result of the most recent United States Postal Service (USPS) rate increase, effective on April 17, 2011, the SCO estimates an increased cost of $61,000 in 2010-11 and $272,000 in 2011-12 and ongoing. Cognizant of the pressures on the GF, the SCO is requesting support for only the reimbursement share of the cost increase through this April letter.

Through an approved 2010-11 budget request, the SCO budget was augmented by $874,000 (various special funds) for projected increased costs in rent and an anticipated increase in postage costs; the total provided was split roughly evenly between the two cost areas. The postage increase did not occur. The SCO reports that the 2010-11 funds for the postage increase have not been spent and will instead be reverted at the end of this fiscal year.

Staff Comment. The SCO's 2010-11 budget was augmented by $442,000 for a postage increase that subsequently did not happen; as noted above, those funds have not been spent and will revert at the end of this fiscal year. On April 17, 2011, a postage increase was implemented.

Staff Recommendation. Approve the April letter.

Issue 2 – Transportation Audits Indirect Allocation Plans

April Letter Request. In an April Finance Letter, the Governor requests continuation of 12.6 positions and $1.751 million (reimbursements) on a two-year limited-term basis to authorize the Controller to continue providing audit services for Indirect Cost Allocation Plans (ICAPs) for Local Government Agencies (LGAs) on an interagency agreement with the California Department of Transportation (Caltrans).

Background. In the 2009-10 budget, the SCO received similar funding on a two-year limited term basis to provide, through an interagency agreement, audit services to Caltrans for audits of ICAPs for LGAs. This request would continue the ability of the SCO to provide these audit services to Caltrans. The ICAP audits are mandated by the Federal Highway Administration of LGAs that receive federal transportation funding. The purpose of an ICAP is to equitably allocate allowable indirect costs of an LGA to benefiting projects/cost objectives through an annual indirect rate. Audits of submitted ICAPs for the last two fiscal years have resulted in a reduction of indirect costs by more than $14 million per year due to discovery of errors and unallowable costs.

Staff Comment. On April 28, 2011, Senate Budget Subcommittee No. 2 on Resources, Environmental Protection, Energy and Transportation approved an April letter from Caltrans for the Caltrans side of this interagency agreement for audit services. The resources requested are limited-term, which is appropriate as the SCO indicates the federal audit requirements may change in future years. In approving this request, staff also recommends inclusion of Supplemental Reporting language to require the SCO report to the Legislature regarding federal audit requirements prior to the next fiscal year with a reporting date of March 1, 2012.

Staff Recommendation. Approve the April letter and supplemental reporting language.

DEPARTMENT OF INSURANCE (0845)

Department Overview. The California Department of Insurance (CDI) regulates the California insurance market and enforces the California Insurance Code, conducting examinations and investigations of insurance companies and producers and working to ensure the financial solvency of companies so that they will meet their obligations to policyholders and claimants. CDI investigates more than 300,000 complaints annually and responds to consumer inquiries. CDI also reviews and approves insurance rates to enforce the statutory requirement that rates are not excessive or unfair. CDI also administers the conservation and liquidation of insolvent and delinquent insurance companies and fights insurance fraud in conjunction with local and state law enforcement agencies.

Budget Overview. The January Governor's Budget provides CDI with 1,338 authorized positions and $224.94 million (Insurance Fund and reimbursements). This is an increase of 71 positions and $16.4 million.

Issue 1 – Workers' Compensation Insurance Fraud Program: Local Assistance Workload Increases

April Letter Request. In an April Finance Letter, the Governor requests increased expenditure authority of $1.646 million (Insurance Fund) local assistance in 2011-12 and ongoing to fund local District Attorney workers' compensation fraud investigation workload increases.

Background. The Workers' Compensation Fraud Program (WCFP) was established in 1991 (Chapter 116; Statutes of 1991), thereby making workers' compensation a felony, requiring employers to report suspected fraud, and establishing a mechanism for funding enforcement and prosecution activities. The Fraud Assessment Commission (FAC) was also established and mandated to annually determine the level of employer paid assessment necessary to fund investigation and prosecution of workers' compensation insurance fraud. Under law, this funding is restricted and cannot be used for any other purpose; after incidental expenses, at least 40 percent of the funds are provided to the DOI Fraud Division for enhanced investigative efforts, and at least 40 percent of the funds are distributed to local District Attorneys. At its September 8, 2010, meeting, the FAC approved an assessment of $31.874 million for local assistance, a 6.5 percent increase over 2010-11 funding. By approving this request, the expenditure authority for the District Attorneys' portion of the WCFP will be appropriately aligned with the current FAC assessment.

Staff Recommendation. Approve the April letter.

CALIFORNIA ALTERNATIVE ENERGY AND ADVANCED TRANSPORTATION AUTHORITY (0971)

For overview and budget information regarding the California Alternative Energy and Advanced Transportation Authority, please see page 31 of this agenda.

Issue 1 – Energy Upgrade California Program

Governor's Request: In an April 1 Finance Letter, the Administration requests an increase of $205,000 in reimbursements for CAEATFA to assist the California Energy Commission (CEC) by providing financial services for the Energy Upgrade California Program (EUC) which is funded by the federal American Recovery and Reinvestment Act (ARRA) of 2009. This request follows the Section 28 request submitted to the Department of Finance in the amount of $4.3 million for the current year.

Background: The CEC received $315 million through ARRA for energy-related projects and rebates. As part of this project CEC developed the EUC, a statewide energy and water efficiency and renewable energy generation retrofit program and contracted with the Local Government Commission (LGC) to run the program. LGC, in turn, has subcontracted with CAEATFA to provide financial services with respect to financial products and lending standards and financial subsidies.

The total amount of the program request is $4,523,000 ($4,318,000 in the current year pursuant to the Section 28 letter and $205,000 as a component of this BCP) through ARRA funding. The funds will be used for staff services, financial subsidy funds, trustee costs, financial advisor services, legal services, travel, and overhead.

This issue is suggested for vote only because the Joint Legislative Budget Committee approved the 2010-11 Section 28 letter for $4.3 million, which represents most of the program funding. The April Finance letter would conform to the JLBC action.

Staff Recommendation: Approve the April letter.

DEPARTMENT OF CONSUMER AFFAIRS (1110)

Departmental Overview and Mission. The Department of Consumer Affair's (DCA) Boards and Bureaus provide exams and licensing, enforcement, complaint mediation, education for consumers, and information on privacy concerns. DCA Boards and Bureaus establish minimal competency standards for more than 255 professions involving approximately 2.4 million professionals. There are currently 25 boards, a commission, three committees, and eight bureaus under the broad authority of the DCA.

Budget Overview. The Boards are budgeted under organizational code 1110, and the total proposed budget is $271.46 million (no GF) and 1,511.3 positions – an increase of $10.4 million and 35.6 positions over 2010-11.

The Bureaus are budgeted under organizational code 1111, and the total proposed budget is $231.34 million (no GF) and 1,386.6 positions – an increase of $14.2 million and 5.7 positions over 2010-11.

Issue 1 – Board of Professional Engineers and Land Surveyors Licensing Exams

April Letter Request. The Governor requests $1.124 million (one-time special funds) for the Board for Professional Engineers, Land Surveyors, and Geologists for fees to the National Council of Examiners for Engineering and Surveying to administer the national examinations to California applicants.

Board of Professional Engineers and Land Surveyors. The mission of the Board for Professional Engineers and Land Surveyors (BPELS) is to safeguard the life, health, property, and welfare of the public by regulating the practice of professional engineering and land surveying. In 2009, legislation was enacted that eliminated the Board for Geologists and Geophysicists and transferred all of the duties, powers, purposes, responsibilities, and jurisdiction to regulate the practices of geology and geophysics to the Board for Professional Engineers and Land Surveyors.

Licensing Exams. The California Business and Professions Code mandates the BPELS to receive applications for licensing, ensure that an exam for licensure is available and accepted in California, and ensure that each exam type is available at least once a year.

Currently, there are 16 different national exams and six state-specific exams for engineers, land surveyors, and geologists offered within California. The National Council of Examiners for Engineering and Surveying (NCEES) develops the national exams used by California. The national exams ensure that individuals licensed in California are accepted for license reciprocity in the other 39 states that use NCEES examinations and out-of-state applicants can gain licensure in California. The exams are administered by BPELS.

Security Breach. In April 2010, the BPELS found that an exam booklet was missing. The NCEES Board determined that the integrity of the exam process had been breached. The NCEES informed the BPELS that if California is to retain access to the national examinations, it must contract with NCEES to administer the examinations. BPELS has a financial liability for all compromised exams, and the amount of the liability varies by exam type. California's liability for the security breach is $2 million, and potential future liability is up to $7.6 million for all national engineering exams provided in California.

Cost of Providing Examinations. Currently, the BPELS administers 22 exams at a cost of approximately $2.45 million annually. This cost includes a $1.8 million contract with NCEES for the use of the NCEES exams. Once BPELS amends state regulations to allow for computerized testing, the contract funds to NCEES will be removed from the BPELS budget, thus saving the state funds in the long-term. After the computerized testing is allowed for, the payment NCEES will receive for administering the exams will come directly from the licensed population in the form of exam fees.

In 2011-12, the one-time funds will pay additional fees to NCEES to administer the exams, while BPELS amends state regulations to allow for a computer-based testing format and lowers the state licensing fees. Additionally, by having NCEES administer the exams, California is released from liability for exam security breaches.

Staff Recommendation. Approve the April letter.

FRANCHISE TAX BOARD (1730)

For overview information regarding the Franchise Tax Board (FTB), please see page 22 of this agenda.

Issue 1 – Data Security and Reliability: Enterprise Tape Library

April Letter Request. The Governor requests shifting $2.29 million approved last year to replace FTB's Enterprise Tape Library from the current year to 2011-12. The expenditure of these funds has been delayed and this proposal would better align the funding to the correct fiscal year. The April Finance Letter is also requesting $2.27 million in 2012-13 to complete the replacement. This delay in expending these funds has not impacted the project costs or the final completion date of the project.

Background. Data security and reliability is critical for FTB given the volume of confidential taxpayer data it maintains. The FTB has employed a defense-in-depth strategy to protect this information where multiple layers of defense are placed throughout its information technology system so that if one fails there are others layers that prevent against a security attack.

Furthermore, the FTB's data reliability is being threatened by outdated equipment and software that is out-of-support. For example, the FTB's Enterprise Tape Library System, which is critical to providing continuous access to the up-to-date accurate information that FTB's automated systems rely on, is at risk of failure. If this system failed, FTB's productivity could be severely hampered and data security could be compromised.

Staff Recommendation. Approve the April letter.

Issue 2 – Voluntary Contribution Funding Codes – Budget Bill Clean-Up

April Letter Request. The April Letter includes amendments to the budget bill to add four new funds and delete four funds that did not meet the voluntary contribution limits required to remain on the state tax return. The four additions that were established by Statutes in 2010 include the following:

- Arts Council Fund
- California Police Activities League (CALPAL) Fund
- California Veterans Home Fund
- Safely Surrendered Baby Fund

The four funds that did not reach the $250,000 threshold for contributions and are proposed to be eliminated include the following:

- ALS/Lou Gehrig's Disease Research Fund
- California Military Family Relief Fund
- California Ovarian Cancer Fund
- Municipal Shelter Spay and Neuter Fund

Background. Current law allows taxpayers to contribute amounts in excess of their tax liability to various voluntary contribution funds listed on the state tax return by checking a box on their California income tax form. These funds must reach the minimum level of $250,000 in their second taxable year. If they do not meet the $250,000 minimum, the law authorizing these fund designations is repealed.

Staff Comments. This proposal is strictly limited to adjusting the budget bill to properly align existing law with the budget bill. The underlying statutes authorizing the voluntary contribution funds are automatically repealed when the minimum threshold is not met.

Staff Recommendation. Approve the April letter.

DEPARTMENT OF REAL ESTATE (2320)

For overview information regarding the Department of Real Estate (DRE), please see page 37 of this agenda.

Issue 1 – SB 36 Mortgage Loan Originator Licensure (SAFE Act)

Governor's Budget Request. The Governor requests $216,000 (Real Estate Fund) and two positions for continued implementation of the federally mandated Secure and Fair Enforcement Licensing Act of 2008 (SAFE Act) which requires states to implement a new licensing program for mortgage loan originators (MLOs).

2010-11 Budget. The 2010-11 budget included $2.8 million (Real Estate Fund) and 27 positions to begin implementation of the SAFE Act.

Prior Subcommittee Action. This request was denied without prejudice at the Subcommittee's January 25, 2011, hearing so that all factors and the DRE's resources could be considered at one time (it was indicated to staff that the DRE might have additional requests related to SAFE Act implementation during Spring budget hearings). Further, the Senate Business and Professions Committee held an oversight hearing on February 28, 2011, focused on DRE enforcement and consumer protection issues. The DRE now reports that there are no additional requests forthcoming with the exception of Issue 1 on page 37 of this agenda, an April Finance Letter related to the relocation and consolidation of the DRE's Headquarters and Examination Center.

Background. The federally mandated SAFE Act requires all states to license and register their MLOs through a nationwide registry called the National Mortgage Licensing System (NMLS). Chapter 160, Statutes of 2009 (SB 36), brought California into compliance with the SAFE Act by requiring those engaging in MLO activities to obtain a license from the Department of Corporations or, if a real estate licensee, obtain a license endorsement from the DRE.

At this point in the SAFE Act implementation process, the main drivers of the additional licensing and enforcement workload for the DRE was the MLO notification in 2010 and ongoing license endorsement renewal process and the annual Business Activities Report and Call Report requirements for all MLO brokers, respectively. With regard to enforcement activities, the workload will be driven by the number of NMLS registrants required to file the mandated reports and the timing of the submission of those reports. More specifically, the Business Activities Reports are first due on a rolling basis beginning on January 2, 2012 (the reports have to be submitted within 90 days after the end of the broker's first fiscal year; April 2, 2012, is the final date these first reports could be filed with the DRE to meet the 90-day requirement). The Call Reports are required to be submitted on a quarterly basis beginning May 15, 2011.

Staff Comment. In approving SB 36, the Legislature approached SAFE Act compliance in a narrow sense by requiring a new endorsement on existing real estate licenses. Licensees pay a $300 fee for that endorsement. Staff notes that while this approach has resulted in the least disruption to existing systems and minimized compliance costs to both the state and licensees, the SAFE Act has represented, and will continue to represent, new workload for DRE. However, due to the timeline when SAFE Act enforcement activities will commence in earnest, the actual workload data is still relatively unknown. Additionally, the DRE has indicated that it is exploring available business analytic technology opportunities to substantially reduce the number of positions needed to review the required reports. The Administration has confirmed that the approach is for the DRE to submit a new comprehensive SAFE Act-related request in a future budget cycle rather than taking a fragmented approach, such as that contained in this request.

Staff Recommendation: Deny the request.

DEPARTMENT OF PERSONNEL ADMINISTRATION (8380)

Department Overview. The Department of Personnel Administration (DPA) is the Governor's chief personnel policy advisor. DPA represents the Governor as the "employer" in all matters concerning state employer-employee relations. DPA is responsible for all issues related to salaries, benefits, and position classification. For rank and file employees, these matters are determined through the collective bargaining process; for excluded employees, these matters are determined through a meet and confer process.

Budget Overview. The January Governor's Budget provides the DPA with 246 authorized positions and $86.4 million ($9.3 million GF). This is an increase of zero positions and $625,000.

Issue 1 – Removal of Recruitment Contract Funding and Language

April Letter Request. In an April Finance Letter, the Governor requests a reduction of $350,000 GF in 2011-12 and removal of provisional budget bill language to reflect the fiscal year 2008-09 expiration of recruitment contracts for medical professionals.

Background. In the 2007-08 Budget, the Legislature approved on a two-year limited-term basis an augmentation of $350,000 GF and provisional budget bill language for recruitment contracts for medical professionals. The funding and language should have been removed in the 2009-10 Budget when the limited-term period expired. For unknown reasons, this action was not taken; therefore, the funding and provisional language remained in DPA's budget.

Staff Comment. According the DPA, the $350,000 GF was not expended in 2009-10 and the DPA reports that it has not and does not intend to spend those funds. However, the DPA does have the ability to still liquidate the funds should they chose to since departments have one year to encumber and two years to liquidate. The 2009-10 funds in question, therefore, could "last" until the end of 2011-12.

With regard to the $350,000 GF contained in the 2010-11 budget, the DPA reports that the funds have also not been expended. Therefore, in its consideration of this request, the Subcommittee may wish to consider adopting budget bill language to revert the 2010-11 funds, as well as the 2009-10 funds, thereby ensuring that the DPA no longer has the ability to access these funds, for additional savings of $700,000 GF.

Staff Recommendation: Approve the April letter to delete the provisional budget bill language and reduce DPA's budget by $350,000 GF in 2011-12; additionally, adopt new reversion items in the 2011-12 budget to realize an additional $700,000 GF savings combined from 2009-10 and 2010-11.

INFORMATION TECHNOLOGY

Issues Proposed for Discussion / Vote

Issue 1 – California Technology Agency (0502) 2009 Governor's Reorganization Plan No. 1

Background. On May 10, 2009, the Governor's Reorganization Plan No. 1 (GRP) took effect thereby beginning the process of consolidating statewide information technology (IT) functions under the California Technology Agency (formerly the Office of the State Chief Information Officer, or OCIO). Since that time, the primary strategic objective has been to transform state government to become more responsive to Californians' needs and to operate more efficiently and transparently through the use of technology.

As required by statute, each year the California Technology Agency (Technology Agency) has updated the state's IT Strategic Plan (first adopted in 2009). The 2011 Statewide IT Strategic Plan streamlines and further clarifies the strategies articulated in the 2009 and 2010 Strategic Plans, and contains the following three strategic goals: (1) Make Government Transparent, Accessible, and Secure; (2) Drive Innovation and Collaboration; and (3) Make Information Technology Reliable and Sustainable Through Consolidated Platforms and Shared Services. In short, and through the implementation of the GRP, the California Technology Agency (Technology Agency) seeks to consolidate the state's IT infrastructure while laying the groundwork for more robust and more sustainable platforms, improve project management practices, oversight, and training, and create an architectural framework to reduce redundancy and improve operations.

Current statute also requires the Technology Agency to produce an annual IT performance report consisting of a variety of assessments and measurements, including the progress made in enhancing IT human capital management, improving the IT procurement process, and enhancing the security, reliability, and quality of IT networks, services, and systems. The Technology Agency is also required to post these performance targets and progress towards these targets to its public internet web site. Finally, current statute requires the Technology Agency to report, at least annually, to the Director of Finance cost savings achieved through improvements to the way the state acquires, develops, implements, manages, and operates state technology assets, infrastructure, and systems.

Chapter 404, Statutes of 2010 (AB 2408) codified the GRP and defined targets and timelines for IT consolidation across the executive branch, including modernizing the state's IT infrastructure to increase efficiency, reduce energy usage, and save costs. With the Technology Agency taking the lead, departments are now required to meet the following mandates: (1) achieve a 20 percent reduction in energy usage by July 2011, and 30 percent by July 2012; (2) achieve a 50 percent reduction in data center raised floor space by July 2011; (3) transition mission-critical and public-facing applications to Tier III data centers and close all other existing server rooms by June 2013; (4) begin migrating from existing network services to the California Government Network no later than July 2011; and (5) begin migrating to the state's shared e-mail solution no later than June 2011.

Chapter 404 also made changes to the IT procurement process to coordinate IT resources across the executive branch. Effective January 1, 2011, departments and agencies are now required to submit IT solicitations (Requests for Proposal) valued at more than $1 million to the Technology Agency and the Department of General Services prior to releasing to the public. Prior to this statutory change, the Technology Agency was not formally included in the IT solicitation process.

Staff Comment. Prior to the adoption of the GRP, state IT had been largely decentralized for years. The GRP, therefore, represented a new and substantial change of course. Since its approval in 2009, Subcommittee No. 4 has annually "checked-in" on the status of its implementation. In those hearings, the Subcommittee focused on examining how IT functions and resources have been streamlined, how statewide IT policies have been standardized, the status of efforts to meet the performance metrics contained in the GRP, and the savings achieved (or to be achieved). All of these areas are valid and the Technology Agency has made great strides in achieving the goals of the GRP; these areas are all also largely captured within existing reports, such as the annual IT strategic plan or other statutorily-required reporting mechanisms. Therefore, as we near the two year anniversary of the adoption of the GRP, and cognizant of the fact that the implementation of the GRP is and will continue to be an evolving process, staff recommends today's discussion focus on what further improvements are needed to what information related to the implementation is collected and how that information is reported and shared to ensure that a complete picture of the implementation is provided on an ongoing basis.

Staff notes that one of the challenges to date with the story of the GRP is that a particular focus has been placed on savings. This is understandable, especially in light of the state's fiscal condition, but it is important to acknowledge that the GRP resulted in some new upfront costs in the early years with likely greater out year savings. This fact likely offset some of the immediate achieved savings. Additionally, capturing IT savings is a challenge as day-to-day IT expenditures are not a defined budget expenditure. Rather, IT expenditures are largely included in departmental Operating Expenses and Equipment funds (and paid to the Technology Agency through rates charged for products and services provided) which makes it difficult to have effective expenditure control mechanisms.

As identified below, it is clear that the Technology Agency is making strides to generate savings though reduced data center square footage, improved energy usage, and decreased server usage, but capturing that savings is difficult (primary reason why savings through a control section is unsuccessful). For example, reducing the data center square footage and the number of servers housed at the data center may result in decreased rates charged by the Technology Agency, but increased storage capacity, staff costs, or usage requests may result in increased rates charged. In this example, if a 3-cent rate decrease is offset by a 3-cent rate increase, the client department sees no change in costs; savings are not captured, but we know the job is being done more efficiently.

This singular focus on savings also misses other key and valid parts of the story where successes have been achieved but have not been reported. For instance, another outcome of the GRP that has proven difficult to quantify are the costs (and risks) that have been avoided in the past two years. The Technology Agency has provided information to staff indicating that, since it was established in 2008 (formerly the OCIO), the state has achieved more than $800 million in savings and cost avoidances through numerous technology initiatives including state-wide IT consolidation, IT Project Oversight, IT Capital Plans, IT Acquisition Plans, annual IT Cost Reporting, and contract renegotiations. Examples of those savings/avoidances include:

- Reduced data center square footage by more than 100,000 square feet. The space savings alleviated the need for a new data center facility, eliminating more than $40 million in capital costs and $24 million in annual operating expenses.
- Identified more than $693 million in cost avoidance through the IT Capital Planning process.
- Reduced IT consultant contracts by $17 million and IT project costs by $52 million through the IT Acquisition Planning process.
- Renegotiated the CalNet 2 contract reducing telecommunications costs to state agencies by $25 million annually.
- Conducted an assessment of wireless rates resulting in more than $3 million in savings to state agencies.
- Reduced data center rates charged to state agencies by $23.94 million:
    - $8 million in rate reductions due to network consolidation.
    - Storage rates have gone down by more than 90 percent since 2008 (from $24 per gigabyte per month to $2 per gigabyte per month).

However, this information on cost (and risk) avoidance is not currently widely reported or shared. Therefore, staff recommends the Subcommittee consider adopting both budget trailer bill and supplemental report placeholder language to improve upon existing reporting metrics to capture these types of additional elements of the GRP implementation efforts. Developed collaboratively with the LAO, Technology Agency, and DOF, the additional metrics would include: (1) reporting on cost (and risk) avoidance and (2) any potential impairments that have been identified to the continued successful implementation of the GRP. Additionally, staff recommends that through the adoption of additional placeholder supplemental reporting language a process be established to convene an annual meeting on the overall status of the implementation of the GRP, and more specifically on lessons learned to date and what barriers to success have been identified. Finally, staff recommends that a copy of the annual report on IT savings also include cost avoidances and that report be transmitted to the Joint Legislative Budget Committee and fiscal committees of both houses of the Legislature.

As the Subcommittee considers these issues, it may wish the Technology Agency and Administration to respond to the following questions:

1. The Technology Agency has identified more than $693 million in cost avoidance through the IT Capital Planning process. What specific examples can the Technology Agency share with the Subcommittee to better delineate these savings? Are there examples of IT projects that were denied? Can the Technology Agency point to an example where the efforts of two departments pursuing similar projects were combined, thereby achieving some measure of economies of scale?
2. One of the functions consolidated in GRP 1 was "human capital management." Could the Technology Agency briefly describe the changes that have been implemented with regard to IT human capital?
3. How has the Technology Agency addressed IT project management in the past year? How has the Technology Agency used project management resources to address projects like 21st Century and FI$Cal (Issue 4 below), which are in process?
4. Savings are either one-time or ongoing. For the savings achieved to date, what percentage is one-time versus ongoing? How will that ratio change over time?

Staff Recommendation: Approve placeholder budget trailer bill language and supplemental report language to improve reporting and information sharing related to the implementation of the GRP.

Vote:

Issue 2 – California Technology Agency (0502) Independent Project Oversight

Governor's Budget Request. The Governor requests $966,000 (Technology Services Revolving Fund) and nine permanent positions for Independent Information Technology Project Oversight (IPO) in 2011-12 and ongoing to meet workload increases and mandated responsibilities of Chapters 183 and 404, Statutes of 2007 (SB 90) and Statutes of 2010 (AB 2408), respectively, and to ensure consistent project implementation of the state's IT projects.

Prior Subcommittee Action. This request was denied without prejudice at the Subcommittee's February 7, 2011, hearing, so that all factors and the Technology Agency's (Technology Agency) resources could be considered at one time (it was indicated to staff that the Technology Agency might have additional related requests during Spring budget hearings). The Technology Agency reports that there are no additional requests forthcoming.

Background. The increased expenditure authority in this request is for a staffing expansion that the Technology Agency considers a critical priority due to legislative mandates, increased public visibility, and the need to ensure consistent project implementation of the state's IT projects. These positions would provide independent project management services to customer departments. These positions are also consistent with the GRP, and its goals of enhancing IT human capital management. The costs associated with the IT project management will be funded by the agency or department administering the project; the Technology Agency would be reimbursed 100 percent by the department or agency requesting the services. Once the Technology Agency has created a professional state governmental entity, comprised of state staff, to manage and direct IT policy, standards, and projects, the state's current reliance on high paid contractors will be diminished. The state currently spends approximately $17.2 million annually on contracted IT project oversight and management.

Staff Comment. The proposed positions represent the beginning of the implementation of the Technology Agency's expanded role as outlined in Chapter 404. Staff concurs that having IPO conducted in-house (as opposed to contracted out) will save the state as the state will eventually no longer rely on highly paid contractors and will instead have developed a cadre of IT professionals within state service.

Staff Recommendation: Approve the request.

Vote:

Issue 3 – Franchise Tax Board (1730) Enterprise Data to Revenue Project

Background. The Franchise Tax Board (FTB) is one of the state's two major tax collection agencies. The FTB's primary responsibility is to administer corporation tax programs and California's personal income tax (PIT). In addition, FTB administers several non-tax-related programs, including the collection of child support payments and other court-ordered payments. The FTB is governed by a three-member board, consisting of the Director of Finance, the Chair of the Board of Equalization (BOE), and the State Controller. An executive officer, appointed by the board, administers the daily operations and functions of FTB.

The Conference Report (SB 69, Budget) passed by the Legislature on March 17, 2011, contains $547.9 million General Fund to support FTB's operations.

The number of personnel-years (PYs) for FTB is budgeted to decline slightly from 5,434 to 5,260.

Tax Gap Reduction Measures

Summary. The FTB estimates that its total tax gap is about **$6.5 billion**. The tax gap is defined as the total tax receipts due to the state less the tax receipts collected by FTB. The department has undertaken several initiatives over the last six years to reduce this tax gap using an enterprise approach. An enterprise approach means that staffs from all different divisions at FTB are involved in reducing the tax gap, including filing, audit, legal, and collections divisions.

1. Enterprise Data to Revenue Project

Background. The FTB's tax filing system has not been substantially updated in the last 25 years. In order to modernize the FTB's filing system, the board initiated the Enterprise Data to Revenue (EDR) Project two years ago. This project will introduce a new PIT and Business Entity return processing system including expanded imaging, data capture, and return validation. Annually, the FTB processes approximately 15 million PIT returns and one million Business Entity returns.

Overall, this project will enable FTB to correct erroneous returns in a timelier manner. It will also be more effective at providing data to identify noncompliance patterns and help identify fraudulent activity. This data system will also allow FTB to better prioritize its workload based on highest cost recovery. The FTB indicates that the new system will also expand self-help tools for taxpayers and tax practitioners to improve the filing and payment activities.

The FTB is using an alternate type of procurement for the EDR project that invites bidders to propose a comprehensive solution to address the overall goals outlined by the EDR project, instead of dictating the solution to the bidders. In this type of procurement, the State enters into a contract with a **Primary Solution Provider (PSP)** and the State works collaboratively with the provider to find a solution that meets the goals of the State. The FTB received proposals last year and chose a PSP in November 2010.

The FTB is also using a **benefits based procurement model** to acquire the EDR Project and get the best value and business driven solution. This model is based on acquiring innovative solutions to strategic business problems and only compensating the contractor when these solutions deliver new tax revenues and after certain State costs are recouped. Revenue benefits are then shared with the contractor up to a fixed contract amount. Furthermore, the contract is constructed so that the State does not incur upfront expenses to compensate the contractor.

When fully implemented, the FTB estimates that the EDR project will bring in over **$1 billion in ongoing revenue annually**. This will help to address the $6.5 billion annual tax gap through increased collection of tax revenues that are due to the State but currently unpaid or uncollected for various reasons. Overall, the **one-time costs of the PSP contract are estimated to be $398.9 million** over the life of the 66-month (5.5 year) contract. This is significantly more than earlier anticipated costs of the project ($234 million). However, the State is now estimating that the proposed solution by the vendor will generate approximately $1 billion more in revenues over the life of the project.

Finance Letter. The Governor's April 1 Finance Letter requests $28.9 million General Fund to support the EDR project in the budget year. Last year, the Legislature approved a $10.2 million request, including 72 new positions. These costs will be more than offset by the additional revenues that the FTB estimates will be received in the 2011-12 fiscal year. The FTB anticipates generating $65.3 million in additional revenues in 2011-12 which is nearly $40 million more than initially anticipated prior to the FTB receiving the PSP solution.

Specifically, the funding requested in the budget year supports the following expenditures:

1. **Personal Services.** Includes $3.9 million for support of personal services. However, no additional positions are provided in this budget proposal. The department has indicated that it will redirect existing vacant positions to support this proposal in the short term.
2. **PSP Contract.** Initial compensation benefits ($25 million) to the PSP paid from additional revenues collected due to the implementation of several "early win" deliverables that will result in additional revenues in the first two to 18 months. Some of the early win deliverables are business process changes that do not require the entire information technology solution to be in place, including making changes to the tax forms to adjust for common mistakes related to real estate deductions and adding additional fields of data to the Accounts Receivable Collection System database.
3. **Independent Verification and Validation (IV&V) Contract.** Funding ($1.3 million) to acquire an IV&V contractor which is a standard practice of the State when entering into contracts for large information technology projects.
4. **Cost Reasonableness Contract.** Funding ($110,000) for Cost Reasonableness consultant services. This consultant will act as another check and balance on the main PSP contract to ensure that the costs charged to the State in delivering the project are reasonable and not outside the normal industry standards.

Staff Comments. Overall, staff finds that the EDR project has been thoroughly planned and the FTB has obviously done significant work to ready the organization for the implementation of the new system, including a complete documentation of their business processes. However, the proposed solution by the PSP has a considerably different cost and revenue structure than originally estimated. It will be critical that the state monitor how the estimated cost and revenue structure of this project tracks with actual revenues and expenditures. Furthermore, the calculation of the revenues attributable to the EDR project is essential to evaluating the relative value of the PSP contract.

- **FTB.** Can you please describe the process you are putting in place to measure what revenues benefits are attributable to the EDR project?
- **FTB.** How will major amendments to the PSP contract be handled if outcomes turn out to be different than estimated?

The Finance Letter assumes that a Section 11 is submitted in the current fiscal year to allow the state to enter into the contract with the PSP. This has not been received.

- **DOF.** What is the status of the Section 11 request for the current year?

Overall success in implementing a new information technology solution requires careful planning and training so that the users interfacing with the system can be successful in transitioning to the new system.

- **FTB.** What steps has FTB put in place to build in redundancy in the system in order to improve outcomes and ensure a smooth transition?
- **FTB.** What steps has FTB taken to ensure adequate training for the workforce transitioning to the new system?

The FTB received authority to hire 72 additional positions to support the EDR project last year. Staff understands that they need to fill an additional 52 positions to support the EDR project in the budget year for a total of 124 positions. The FTB has not received authority to hire 52 new positions in the budget year and is planning to redirect vacant positions internally to address the EDR workload. The April Finance Letter includes $3.9 million General Fund to support these redirected positions because these redirections would bring FTB's vacancy rate below 5 percent. (It is standard state budgeting practice to assume 5 percent [salary] savings when funding positions.) The FTB indicates that the redirection can be managed in the interim, but staff finds that the ongoing success of the project could be jeopardized if the implementation of the EDR solution is significantly under resourced – potentially leading to a pennywise pound foolish result. Furthermore, other revenue generating aspects of FTB's operations could be negatively impacted by the redirection.

- **FTB.** What are the main categories of staff needed to implement the EDR solution?
- **FTB.** Will these redirections have an impact on FTB's operations?

Staff Recommendation. Hold this issue open pending receipt of the 2010-11 Section 11 request.

Issue 4 – Financial Information System for California (FI$Cal) (8880) Budget Request for 2011-12

Department Overview: The Financial Information System for California (FI$Cal), is an Enterprise Resource Planning (ERP) information technology (IT) project intended to replace, consolidate, and upgrade multiple legacy financial systems with a single system that would encompass the areas of: budgeting; accounting; procurement; cash management; and financial management. The development of FI$Cal resides with four "Partner Agencies": the Department of Finance, the State Treasurer's Office, the State Controller's Office, and the Department of General Services. The FI$Cal system will be implemented in several phases, or "waves," over the next decade. Budget Control Section 8.88 is a technical fiscal provision that directs special funds to the FI$Cal project and it will be made to conform to the final budget adopted under the 8880 budget items.

January Budget Overview: The January Governor's budget proposed $70.8 million ($20.9 million GF) for continuing the FI$Cal project. This represents a year-over-year increase of $29.0 million ($5.2 million GF). Funded positions would grow from 62.1 to 95.9. The reason for the funding increase is that the project would be moving into the implementation stage with contract award to the vendor by December 31, 2011. The 12-year cost of fully implementing the project is estimated at $1.6 billion (both GF and other funds). The Administration is exploring financing options such as bonding and vendor-financing to spread costs over a longer period.

Current Budget Status: In February, the Subcommittee maintained the funding level proposed by the Governor, but indicated the FI$Cal budget would be reviewed further and heard again in the spring. The Subcommittee expressed concern about the GF cost of the FI$Cal project given the budget shortfall.

Governor's Revised Budget Request: The Administration has issued a Spring Finance Letter that redefines the budget year request for the FI$Cal project to reduce costs in 2011-12 and reflect the new project schedule. The new request reduces the requested funding for the budget year by $32.4 million ($18.4 million GF), and pushes the project schedule back by about 4 months. The revised budget proposed for 2011-12 is $38.5 million ($2.5 million GF). The request for 33 new positions made in January, would also be withdrawn.

Project Timeline: Currently, three selected vendors are completing the "Fit-Gap," or stage I contract, which involves a review of potential gaps between the vendor's software and the state's business requirements. Project staff have also asked the three vendors to propose financing options and have held discussions with the State Infrastructure Bank (I-Bank) on financing options. The following are key upcoming dates, as revised in the April Finance Letter:

- **June 2011** – Proposals due from the competing vendors.
- **January 2012** – Submission of Report to the legislation outlining the proposed vendor and IT solution.
- **April 2012** – Award of system contract (contingent on legislative support).

Project Financing: The FI$Cal project has produced a white paper on funding options. The paper outlines the following three options for financing the FI$Cal project:

- **Pay-Go**: Fund project costs in the budget as these costs are incurred, which results in the lowest overall project costs, but requires huge up-front costs in 2012-13 to 2017-18;
- **Vendor Financing**: Some of the contract costs would be financed through the vendor to help reduce the initial costs and spread out the costs over an additional five years; and,
- **I-Bank/Bond Financing**: Provides the lowest up-front costs, but has the highest overall costs by spreading costs over 15 years.

Staff Comments: The FI$Cal project is a multi-year effort which is completing its third year as a stand-alone budget item. Fiscal year 2011-12 is a pivotal fourth year for the project, in which the Administration will select a preferred product and partner, as well as a financing plan. The Administration will present the proposal to the Legislature for their review in the winter and spring of 2012. To the degree the solution proposed next year has the Legislature's support, the fiscal cost in 2012-13 can be managed through defining the speed of the roll-out and the financing strategy.

Staff Recommendation: Approve the FI$Cal budget as modified by the April Finance Letter.

Vote:

Issue 5 – Secretary of State (0890) California Business Connect Project: Phase I

April Letter Request. In an April Finance Letter, the Governor requests one-time increased expenditure authority of $1.16 million (Reimbursements) for Phase I of the California Business Connect Project, scheduled to begin in July 2011 with a projected completion date of June 2016.

Prior Budget Actions. Initially funded in 2001, with total project costs of $33.6 million (roughly $31.6 Business Fees Fund with remainder from the Business Reinvestment Fund) the Legislature approved the SOS's Business Automation (BPA) Project, which was expected to automate and modernize business processes. The BPA was approved for two phases, with Uniform Commercial Code (UCC) filings and other lien-related filings as the first phase and Business Entities, Special Filings, and Trademarks as the second phase. The BPA resulted in the customization and modification of a commercial-off-the-shelf product to support the statutory and business requirements for UCC and other lien-related filings. After the UCC phase was implemented in 2006, the vendor notified the SOS that their business model had changed; therefore, the BPA scope was reduced to the first phase only. As of January 1, 2010, the BPA vendor no longer provides maintenance and operational support for the UCC system; replacement of this system is scheduled in the final phase of the Business Connect project.

The 2010-11 budget included $1 million (Business Fees Fund) over two years to reduce the current backlog of Business Entity Filings and Statements of Information applications in the Business Programs Division. Of the $500,000 available under each year of the plan, $250,000 is for short-term information technology (IT) improvements to increase the functionality of the current electronic filing system and $250,000 is for staffing costs. When this two-year plan was adopted, the SOS indicated that it was intended to dovetail into a future IT project which would serve as the long-term solution to automate the Business Program Division.

Background. The SOS is responsible for the administration and enforcement of laws pertaining to filing documents associated with corporations, limited partnerships, and perfecting security agreements. On an annual basis, the SOS' Business Program Division (BPD) receives over a million business filings and requests a year. These filings by businesses are statutorily required and are not effective until reviewed and filed by the SOS. The filings and requests are comprised generally of two categories: (1) Business Filings, required of corporations, limited liability companies, and limited partnerships, which include such documents as articles of incorporation, trademarks, and other special filings; and (2) Statements of Information, which are required on an annual basis for corporations and on a biennial basis for limited liability companies, and also include common interest development association statements and publicly traded disclosure statements. Business filers are currently charged from $15-$150 dependent on the type of filing. Businesses can also pay additional fees to receive expedited service, such as $350 for 24-hour turnaround or $750 for same-day service.

The current process for accounting for and accepting these filings and requests is labor-intensive and reliant on several antiquated legacy computer systems, as well as a "paper" database (index cards) system. The SOS utilizes 23 separate Information Technology systems to support 15 of the filing types; the remaining eight filing types are essentially paper-based manual systems supported only with basic automation tools, such as Microsoft Word and Excel.

In May of 2009, the BPD had a backlog of 4,752 Business Filings with a 22-calendar day wait time; Statements of Information had a backlog of 36,737 filings with a 15-calendar day wait time. After the 2009 budget line-item veto which represented a 10 percent reduction to all constitutional offices including the SOS, and in May 2010, the Business Filings backlog had increased to 30,093 with a 72-calendar day wait time; the Statements of Information backlog had increased to 89,322 with a 52-calendar day wait time. In October of 2010, the backlogs had grown to 117-calendar days for Business Filings and 101-calendar days for Statements of Information.

As noted above, as part of the 2010-11 budget, a $1 million two-year plan was adopted to reduce the current backlogs in the BPD. As of April 11, 2011, the SOS reports that $300,000 has been spent, resulting in the processing of 94,000 Business Filings with $2.8 million in filing fees attached. This activity reduced the Business Filings backlog by over six weeks (from 117-calendar days to 72-calendar days). The funding was utilized to keep the backlog in Statements of Information relatively flat (the backlog in October 2010 was 101-calendar days; the April 2011 backlog is 111-calendar days). Progress was not made in reducing this backlog because the annual volume of filings is so large.

As of April 11, 2011, the current BPD backlog totals 200,000 documents waiting to be processed; of these, roughly 70,000 are Business Filings, with the remainder Annual Statements of Information. The SOS estimates that $3 million in uncashed checks are attached to these filings. Depending on type of filing, the current wait time is from two to four months.

The Business Connect Project is proposed as a business- or solutions-based procurement whereby vendors are provided with a business case and fundamental requirements which they then propose and submit solutions to meet the SOS' needs. Phase 1 consists of the development of the SOS' business and functional requirements which becomes the Request for Proposal (RFP) that vendors then respond to. More details about the technical solution, including a more robust estimate of project costs, will be outlined in a Special Project Report (SPR) to be filed with the California Technology Agency after vendor responses to the RFP are received. Based on the approved SPR, additional spending authority for each subsequent phase of the project will be sought from the Legislature. The SOS estimates total project costs of $23.7 million. The fund source is fees currently paid by businesses for filings and services.

Since 2006-07 and through 2009-10, both Reimbursements (expedited and special handling fees) and Business Fees Revenues (standard filing fees) have represented a GF solution totaling $23.1 million and 40.7 million, respectively. In 2010-11, it is estimated that $9.2 million in Reimbursements and $1.1 million in Business Fees Revenues will transfer to the GF. In 2011-12, it is projected that $9.0 million in Reimbursements and $432,000 in Business Fees Revenues will transfer to the GF. Figures 1 and 2 below provide further detail as to these collections and GF transfers.

Figure 1
Reimbursements Collected and Transferred to the GF (dollars in thousands)

	2006/07	**2007/08**	**2008/09**	**2009/10**	***2010/11 Estimated***	***2011/12 Projected***
Revenues	$13.4	$13.0	$11.4	$14.0	*$16.2*	*$16.2*
Expenditures	$7.3	$7.3	$7.3	$6.8	*$7.0*	*$7.2*
Total Excess Transferred to GF	$6.1	$5.7	$4.1	$7.2	*$9.2*	*$9.0*

Figure 2
Business Fees Fund Revenues Collected and Transferred to the GF (dollars in thousands)

	2006/07	2007/08	2008/09	2009/10	*2010/11 Estimated*	*2011/12 Projected*
Revenues	$51.0	$47.0	$44.4	$38.9	*$39.5*	*$39.5*
Expenditures	$32.4	$36.3	$35.8	$36.1	*$38.4*	*$39.1*
Total Excess Transferred to GF	$18.6	$10.7	$8.6	$2.8	*$1.1*	*$.4*

Staff Comment. The Business Connect Project has merit. The existing process is inefficient, the current legacy systems present a challenge to operate and maintain, and that the current backlog does not help the state's business climate. While the fees businesses have been paying have represented a GF solution in recent years, these fees were not paid with that intent. The SOS also estimates that the Business Connect Project, when complete, will save the state $5.6 million per year which means the costs of the project could be recouped in a fairly expedient manner.

Staff notes, however, two concerns with the proposed project. First, with regard to the fund source, as noted above the primary funding source for this project are the expedited fees paid by businesses. While a relatively stable revenue source in recent years, the majority of this revenue can be directly correlated to the length of the backlog; i.e., the larger the backlog the more likely a business will pay an expedited fee. The two-year $1 million solution adopted in 2010-11 has reduced one of the backlogs in question by nearly one-third via the expenditure of only 30 percent of the total funding appropriated. At some point, as the remaining $700,000 is expended on the two-year solution, a "tipping point" will be reached where the backlog will be low enough that businesses will no longer be paying the expedited fees at current rates of payment. This raises questions about the viability of this fund source to sustain the project's costs through its completion in 2016. Further, the "backstop" funding source, Business Fees Fund Revenues (Figure 2 above) is not much of a backstop as it has declined markedly in recent years with a 2011-12 projection of only $432,000 available for transfer (or expenditure on the Business Connect Project). This uncertainty places the GF at risk for being the true funding backstop for this project.

Second, staff notes that the current estimate of project costs is just that, an estimate, and there is not presently a level of certainty of what this project will actually cost. The FSR states the SOS conducted extensive monitoring and market research, and determined that the state with the closest system to meeting the SOS' needs was in North Carolina, yet that solution would only meet 30 to 40 percent of the SOS' needs, handles a significantly smaller volume, and has government accounting systems significantly different than California's. Therefore, the SOS reached the conclusion that a solutions-based procurement was necessary. This is a reasonable conclusion, but it translates to a level of uncertainty about costs estimates. This is not a criticism about the Business Connect Project or the materials presented by the SOS, but rather the reality of the state's process for developing this type of information technology project. Until an FSR is approved, a detailed RFP is developed, vendors bid on that RFP, which in turn drives the SPR which is submitted to the Technology Agency for its approval, a true estimate of the project's cost will not be fully known.

If the Subcommittee were to approve this request as presented it is in essence providing tacit approval for the entire Business Connect Project. Given all the factors at work, including that a true estimate of project costs is not known and there are questions about the viability of the fund source (and what impact the remaining $700,000 of the two-year solution will have on the stability of this fund source over time), providing approval of the entirety of the Business Connect Project at this juncture may be premature. Rather, in considering this request, the Subcommittee may wish to make clear it is only approving the development of the RFP, through the completion of the SPR. This would allow the Subcommittee to have at its disposal a more accurate estimate of project costs, as well as a more complete understanding of the viability of the fund source, when considering the Business Connect Project as part of a future budget cycle.

Staff Recommendation. Approve only the development of a Request for Proposal and the subsequent development of a Special Project Report for the Business Connect Project.

Vote:

0971 CALIFORNIA ALTERNATIVE ENERGY AND ADVANCED TRANSPORTATION AUTHORITY

Department Overview: The mission of the California Alternative Energy and Advanced Transportation Financing Authority (CAEATFA) is to promote the prompt and efficient development of energy sources which are renewable or which more efficiently utilize and conserve scarce energy resources.

January Budget Overview: The January Governor's Budget proposed total funding of $25.8 million (special funds and reimbursements) and 7.0 positions, an increase of $9.2 million and no change in positions. The year-over-year increase is primarily explained by the implementation of California Ethanol Producers Incentive Program. (See Issue 2 on the following pages for detail on this budget request).

Current Budget Status: One April Finance Letter was proposed, which is Issue #1 below.

Issue Proposed for Discussion / Vote

Issue 1 – AB 118 / California Ethanol Producers Incentive Program

Governor's Request: The Administration requests $9 million in reimbursement authority for CAEATFA to receive funds from the California Energy Commission (CEC) to perform activities related to the Alternative and Renewable Fuel and Vehicle Technology Program as authorized by AB 118 (Chapter 750, Statutes of 2007, Nunez). The specific program is the California Ethanol Producer Incentive Program (CEPIP) whereby financial assistance is provided to ethanol producers selected by CEC to develop and commercialize advanced transportation technologies that meet advanced energy goals.

Background/Detail: CAEATFA and the CEC entered into an interagency agreement that outlines the terms by which CAEATFA will assist CEC in implementing the ethanol incentive program goals. The interagency agreement is expected to have a 4-year term expiring in January 2015. The terms of the agreement allow a transfer from the CEC to CAEATFA of up to $15 million. To date, a total of $6 million has been transferred. The Governor's budget reflects a $15 million reimbursement in 2010-11 and a $9 million reimbursement in the budget year. The two-year amount requested exceeds the interagency agreement by about $9 million – CAEATFA indicates this is proposed due to uncertainty about how funds will be distributed across fiscal years, so they double-counted the $9 million.

February 10, 2011, Hearing: This issue was rejected without prejudice to allow further time for review and to consider the March 2011 AB 118 report.

Draft AB 118 Report: This year's report has been released by the CEC and states the following on the Ethanol Producers' Program:

During the administration of the CEPIP, market conditions have become increasingly unfavorable for ethanol production, particularly within California. This is due in part to near record commodity costs for corn. Given uncertain market conditions and future price projections, it is unclear whether a modest state price support program can offset the impacts of this *unprecedented change in the ethanol fuel market. As a result, the Energy Commission will reevaluate the future of the CEPIP and study the benefits from its proposed $6 million investments before making a recommendation on funding.*

Staff Comment: Given the comments in the CEC report, there are likely more cost-effective ways to expend AB 118 dollars. If the $9 million request for 2011-12 is rejected, CAEATFA and CEC can evaluate the program results for the initial $6 million and CEPIP funding could be considered again next year, if warranted.

Staff Recommendation: Deny the BCP.

Vote:

0840 STATE CONTROLLER'S OFFICE

Department Overview. The State Controller is the Chief Fiscal Officer of the state. The primary functions of the State Controller's Office (SCO) are to provide sound fiscal control over both receipts and disbursements of public funds; to report periodically on the financial operations and condition of both state and local government; to make certain that money due the state is collected through fair, equitable, and effective tax administration; to provide fiscal guidance to local governments; to serve as a member of numerous policy-making state boards and commissions; and, to administer the Unclaimed Property and Property Tax Postponement Programs.

Budget Overview. The January Governor's Budget provides the SCO with 1,491 authorized positions and $218.9 million ($76.5 million GF). This is an increase of two positions and $65,000.

Issues Proposed for Discussion / Vote

Issue 1 – Local Government Oversight Initiatives

April Letter Request. In an April Finance Letter, the Governor requests increased expenditure authority of $2.098 million (reimbursements) to support 16.4 existing positions to provide increased oversight of local government entities under the SCO's existing statutory authority.

Background. Generally speaking, direct state oversight of local governments is currently limited to state and federal pass-through funding. Counties receive a large share of state/federal pass-through funding to administer a number of statewide programs under state supervision, such as health and welfare. As a result, they receive direct state oversight, including SCO audits. For cities and special districts, state oversight is more limited to the few grants or allocations of state/federal pass through funding, such as Gas Tax allocations, distributed by the state. In addition, current statute provides for a more indirect oversight of local government funding using the following three elements:

1. <u>Annual Audits</u>. Each local government entity is required to have an annual audit performed by an independent auditor. If the local government has over $500,000 in federal expenditures, it must also have a single audit. Local governments are required to submit these audits to the SCO. The SCO can initiate a quality control review of the work papers of any auditor when there is suspicion that the work performed is inadequate.
2. <u>Financial Transaction Reports</u>. Statute requires the SCO to collect a report of annual financial transactions from each county, city, and special district and to publish them in reports available to the Governor, legislature, and general public. Statute further provides that, if the reports are not made in the time, form, and manner required, or if there is reason to believe a report is false, incomplete, or incorrect, the SCO shall appoint a qualified accountant to make an investigation and to obtain the information required. Statute specifies that the SCO's enforcement costs are to be reimbursed by the local government entity in question.
3. <u>Accounting and Audit Guidelines</u>. Uniform accounting guidelines are intended to provide local governments with the information necessary to implement and operate a common

accounting and reporting system. Currently such guidelines are only required for counties and special districts.

With regard to the Financial Transaction Reports, these reports represent the only source of available statewide financial data on local government entities. According to 2010 estimates, the SCO staff spent more than 1,100 hours annually on monitoring the submissions and collecting forfeitures (required payments to the state for failure to file the financial report with the SCO). The SCO indicates that the reports are subject to automated edits that do not necessarily identify all the issues that warrant attention. For instance, the SCO does not presently have the resources to compare these reports between years or between similar entities. In addition, the current analyses of all of the complaints that are being submitted to the SCO (since the City of Bell stories were reported last year) are being done through staff redirections. To the extent that an analysis results in a need for further investigation, additional redirections would be needed.

Staff Comment. The current approach is not working at an optimal level to protect taxpayers from waste, fraud, and abusive financial practices. Perhaps the greatest area where more could be done is with the financial transaction reports. This request would address that need by providing the resources to the SCO to investigate and prepare annual financial transaction reports for all non-filers, as well as conduct investigations of individual financial issues that indicate some information in an annual transaction report is "false, incorrect, or incomplete."

In considering this request, it is important to note that this request would effectively expand the use of the SCO's current statutory authorities to provide more comprehensive and coordinated oversight of local government financial practices. In theory, this would identify problems before they reach a critical stage. However, the SCO has not provided a detailed systematic plan for how it would execute the additional activities nor provided any detail regarding a benefit/cost assessment of additional financial monitoring. The audit plan submitted by the SCO is limited to a total of 47 non-filing cities and special districts for 2009-10. Based on this limited universe, the justification for funding the full request and 16.4 positions is unclear. Therefore, staff recommends this request be held open pending receipt of the requested information from the SCO.

Staff Recommendation: Hold open pending receipt of additional information.

Vote:

Issue 2 – 21st Century Project: Related Language

April Letter Request. In an April Finance Letter, the Governor requests budget trailer bill language, as well as amended 2011-12 provisional budget bill language, to ensure deployment of the 21st Century Project.

Prior Subcommittee Action. On January 25, 2011, the Subcommittee approved $63.7 million ($34.2 million GF, $1.0 reimbursements, and $28.4 million special funds) to fund the 21st Century Project in 2011-12.

Background. The SCO pays approximately 249,000 employees, including state civil service, California State University and Judicial Council employees, judges, and elected officials. The

21st Century Project (Project) will replace the existing statewide human resource management systems in order to improve management processes and fulfill payroll and reporting obligations accurately and on time. The Project began in May 2004. The first deployment wave is scheduled for October 2011, comprised of 25 departments and 14,281 employees. That initial wave will be followed by three successive wave rollouts in January 2012 (50 departments and 75,841 employees); July 2012 (10 departments and 68,065 employees);and October 2012 (77 departments and 84,650 employees). The current estimated total cost (one-time and continuing) of the 21st Century Project is $303.2 million.

This request includes the following statutory changes related to the 21st Century project:

1. Amend Section 12432 of the Government Code to extend the SCO's existing authority to assess a variety of state funds to support the completion of the 21st Century Project. Existing law would repeal this provision on June 30, 2011. The proposed budget trailer bill language would extend the date until June 30, 2014, a date consistent with the completion of the project.
2. Amend Section 3527 of the Government Code to include a limited number of positions in the SCO's Information Systems Division (ISD), and incoming staff transfers from the 21st Century Project to the ISD, to receive and/or continue their "excluded" designation following the successful deployment of the 21st Century Project.
3. Amend Section 12420.1 of the Government Code to limit the SCO's responsibilities related to establishing employee-requested deductions for the purpose of purchasing savings bonds through the Federal Treasury Direct Program with the deployment of the 21st Century Project.

The request also includes modification of existing provisional budget bill language to allow for additional 21st Century Project funding of up to $5 million in a current fiscal year due to unforeseen circumstances and if required to ensure the successful deployment of the system. The modified language does not alter an existing requirement that the Legislature be notified in writing 30 days in advance of any adjustment being made.

Staff Comment. Budget trailer bill language is the implementing language of the California State Budget Bill. While the 21st Century Project has been, and will continue to be, funded in the annual budget act, except for the amendments to Section 12432 of the Government Code, staff has been unable to identify a direct connection between the 2011-12 budget and the other two requested amendments.

The modified provisional budget bill language is intended to address unforeseen circumstances that could arise as the 21st Century Project reaches the final stages of implementation. It provides a limit and some transparency through existing legislative notification requirements; however, there are no criteria included to indicate when such an adjustment could occur or why the SCO needs such delegated authority at this time. In addition, this modified language would set the precedent of permitting an IT project to spend up to $5 million more than its approved budget or project documents without going through some form of a budget, bill, or deficiency process. Therefore, while staff recommends adopting the modified language it would be only with a lower cap of $2 million and with supplemental report language requiring the DOF and Technology Agency, in consultation with the LAO, to develop written criteria regarding the use of this authority in the future and implement the criteria prior to the commencement of the 2012-13 budget process.

Staff Recommendation: (1) Approve the modified provisional budget bill language but with a $2 million limit and placeholder supplemental report language; (2) Approve the proposed trailer bill language amending Government Code Section 12432; and (3) Deny without prejudice the remaining proposed budget trailer bill language with direction that those changes be pursued in a policy bill.

Vote:

2320 DEPARTMENT OF REAL ESTATE

Department Overview. A primary objective of the Department of Real Estate (DRE) is to protect the public in real estate transactions and provide licensing, regulatory, and subdivision services to the real estate industries. The DRE is entirely special funded (Real Estate Fund) and derives its revenues from examination, license, and subdivision fees. The core functions of the DRE are to administer license examinations, issue real estate licenses, regulate real estate licensees, and qualify subdivision offerings.

Budget Overview. The January Governor's Budget provides DRE with 381 authorized positions and $46.0 million (RE Fund and reimbursements). This is an increase of two positions and $1.5 million.

Issue Proposed for Discussion / Vote

Issue 1 – Sacramento Headquarters and Examination Center Consolidation and Relocation

April Letter Request. In an April Finance Letter, the Governor requests increased expenditure authority of $2.612 million (Real Estate Fund) to relocate and consolidate into one location on or about January 1, 2012, the DRE's Sacramento Headquarters Office and Examination Center. Figure 3 below summarizes the components of this request:

Figure 3

	2011-12	2012-13	2013-14
Six months rent increase January 1 through June 30, 2012	$635,500*		
Moving related expenses	$1,220,000*		
Tenant Improvements	$756,000*		
Increased rent costs for twelve months (July 1, 2012, through June 30, 2013)		$1,271,000	
Six months of scheduled lease cost increase ($.07 per square foot of office space)		$31,500	
Ongoing lease cost increases over term of lease			$63,000
TOTAL	$2,611,500*	$1,302,500	$63,000**

*2011-12 costs are all one-time.

**Increased amount continues through Fiscal Year 2019-20.

Prior Subcommittee Action. As part of the 2009-10 budget, the Governor requested a one-time augmentation of $1 million (Real Estate Fund) to partially cover the estimated costs ($1.3-$1.5 million) to relocate and consolidate the DRE's downtown Sacramento Headquarters Office and Examination Center at a new location. At that time, staff did not necessarily dispute DRE's claim that the existing facilities did not meet the long-term needs of the department and once increased rent and the cost of a double move were factored in. However, the Subcommittee rejected the request due to the fact that the Real Estate Fund had a structural deficit.

As part of the 2010-11 budget, the DRE did not present a request related to its Headquarters relocation and consolidation; rather, the DRE proposed to absorb those costs from within its existing budget. The Subcommittee did not agree with this approach, due to concerns that doing so could result in decreased enforcement and consumer protection activities. The Subcommittee instead requested that the DRE present a formal request related to its facility needs during the 2011-12 budget process.

Background. The DRE's Headquarters and Examination Center facilities have been located in their present locations in downtown Sacramento since 1985. The DRE leases a total of 44,922 square feet at a cost of $1.75 per square feet. The current lease expires on September 30, 2011, and will thereafter convert to a month-to-month soft-term lease agreement. The amount of leased space has not changed during the 26 years the DRE has been at this location; therefore, the current facilities present significant space constraints. Since 1985, the DRE's licensee population and the associated workload and file storage requirements have increased by 70 percent; there were 268,842 licensees in 1985, and a total of 457,113 today. In addition, the DRE was recently required to add a new licensing and enforcement program for mortgage loan originators. The DRE has also absorbed a 38 percent increase in staff levels, from 144 staff in January 1987 (accurate earlier data unavailable) to a total of 198 today. In addition, the current facilities present significant health and safety concerns and deterioration problems. The DRE also cannot offer electronic license examinations in the current exam center without extensive renovations and costs; current estimates are that the costs could approach $900,000 based on renovations of similar exam facilities.

Working with the DGS' Real Estate Leasing and Planning Section, the DRE is considering several new locations within the City of Sacramento, as required by current law. The request before the Subcommittee represents a new facility comprised of a total of 75,000 square feet of office space at an estimated cost of $2.40 per square foot and 10,000 square feet of warehouse space at an estimated cost of $.45 per square foot, for a total estimated lease cost of $2.214 million per year. The DRE is presently paying $943,000 per year for its current facilities; the new location would therefore represent a net increase of $1.271 million per year in lease costs. The DGS is proposing a lease term of eight years, with the first four years termed "firm," and the second four years termed "soft." According to DGS, the eight year lease is a state product and has been in use for about ten years.

The one-time moving costs are estimated to total $1.22 million, including: (1) $990,000 for Modular Systems Furniture; (2) $115,000 in moving expenses; (3) $46,000 to install telecommunications systems; (4) $46,000 for network switches, cabling, and electrical costs; and (5) $23,000 for supplies such as business cards, stationary, etc.

Staff Comment. Staff concurs with the need to relocate and consolidate the DRE's Sacramento Headquarters and Examination Center facilities into a single location, thereby achieving a more efficient operation and a safer working environment, for both employees, licensees, and the general public. Remaining in the current location is not an option, neither is renovating the current facility as that option would require costly improvements and do nothing to address the fact that the DRE has simply outgrown its current space. This latter option would also involve double moving costs.

Staff notes that this request is built upon estimated lease costs of $2.40 per square foot for office space and $.45 per square foot of warehouse space. The DGS has indicated, however, that given current conditions in the commercial real estate market it is likely that DRE's office lease costs will result in a final cost of $2.00 per square foot, with a similar level of reduction in warehouse lease costs. Therefore, in considering this request, the Subcommittee may wish to adopt provisional budget bill language to ensure that any unused funds appropriated in 2011-12 for lease terms are not built into the DRE's base budget.

Staff Recommendation: Approve the request and adopt placeholder provisional budget bill language to state that the DRE cannot redirect amounts in excess of agreed-upon relocation and consolidation costs, including lease terms, to other purposes.

Vote:

8955 CALIFORNIA DEPARTMENT OF VETERANS AFFAIRS

Department Overview. The California Department of Veterans Affairs (CDVA) promotes and delivers benefits to California veterans and their families. More specifically, the CDVA provides: (1) California veterans and their families with aid and assistance in presenting their claims for veterans' benefits under the laws of the United States; (2) California veterans with beneficial opportunities through direct low-cost loans to acquire farms and homes; and (3) the state's aged and disabled veterans with rehabilitative, residential, and medical care and services in a home-like environment at the Veterans Homes of California (VHCs). The CDVA operates VHCs in Yountville (Napa County), Barstow (San Bernardino County), Chula Vista (San Diego County), and Greater Los Angeles Ventura County (with homes in West Los Angeles, Ventura, and Lancaster).

Budget Overview. The January Governor's Budget proposes to continue to ramp-up admissions at the VHCs in West Los Angeles, Lancaster, and Ventura. The Governor also proposes to provide continued resources and staffing related to the construction and activation of two new VHCs, in Redding and Fresno, both of which are scheduled to begin admissions in early calendar year 2012. The January Governor's Budget provides CDVA with 2,396.5 authorized positions and $399.3 million ($253.4 million GF).

Issue Proposed for Discussion / Vote

Issue 1 – Central Coast Veterans Cemetery Project: Preliminary Plans

April Letter Request. In an April Finance Letter, the Governor requests that two new items be added to the 2011-12 budget to transfer and then appropriate $1.074 million for the preliminary plans phase of the Central Coast Veterans Cemetery project.

Background. Military and Veterans Code Section 1450 et seq. required the CDVA to develop a master plan for a Central Coast Veterans Cemetery Project, a state-owned and operated veterans' cemetery on the grounds of the former Fort Ord in Monterey County. To fund the Cemetery Project, the original 2000 statute provided $140,000 GF seed money for the master plan and created two funds: (1) the California Central Coast State Veterans Cemetery at Fort Ord Endowment Fund (Endowment Fund); and (2) the California Central Coast State Veterans Cemetery at Fort Ord Operations Fund (Operations Fund). The Endowment fund is the mechanism for local entities to provide funding for the development and operation of the Cemetery Project. The Operations Fund receives its funding via transfer from the Endowment Fund to support the costs of designing, constructing, and maintaining the Cemetery Project. To protect the state, and before a transfer can be made, statute requires a Director of Finance determination that adequate funds exist in the Endowment Fund to fully complete the preliminary plans (as well as working drawings).

Per the master plan, the Cemetery Project would utilize a portion of a 79-acre site and accommodate the remains of nearly 14,000 veterans and spouses. It is expected that the Cemetery Project would accommodate anticipated burials for the next 20 years and that the full 79-acre site, once eventually developed, is adequate to meet burial demand for the next 100 years. The total Cemetery Project costs of $27.0 million would be funded through a mixture of local moneys transferred into the Endowment Fund and federal funds, with the federal funds providing all of the construction costs and reimbursement of most of the design costs.

The April letter before the Subcommittee would add item 8955-011-0848 to the 2011-12 budget to transfer $1.074 million from the Endowment Fund to the Operations Fund. In addition, the April letter requests that item 8955-301-3013 be added to the 2011-12 budget to appropriate $1.074 million from the Operations Fund for the preliminary plans phase of the Cemetery Project.

Statute also requires the State Controller's Office to annually report the amount of interest and investment earnings generated by the Endowment Fund and the estimated amount of additional principal needed to generate annual interest revenue that will sufficiently fund the estimated annual administrative and oversight costs. The most recent report, dated July 22, 2010, reported that no deposits were made to the Endowment Fund and the fund remained with a zero cash balance for the fiscal year ended June 30, 2010, and prior. Therefore, no interest or investment earnings were generated.

Staff Comment. This April letter requests to add items to the budget to transfer nonexistent funds from an Endowment Fund to an Operations Fund and then appropriate those nonexistent funds to cover the costs of preliminary plans for the Central Coast Veterans Cemetery Project. When queried on this approach, the Administration indicated that while it is not commonly utilized its purpose is to show good faith on the part of the state with the local entities that support and are raising funds for the Cemetery Project. The local entities presently fear that if they deposit funds raised (currently $160,000) into the Endowment Fund they have no assurance that the state will then in turn appropriate the funds for preliminary plans, which is the first phase or step to realizing the Cemetery Project. Given the state's fiscal condition, this fear is understandable, and has also potentially impacted the local entities' ability to raise funds. Were this request to be approved, local entities could therefore have an enhanced ability to raise funds as they have "proof" of the state's intent to support the Cemetery Project.

According to the Administration, this approach was used in the 2001-01 budget to authorize a predominantly privately funded project to renovate and expand the Lincoln Theater at the Veterans Home of California Yountville prior to the private funds being in place. More recently, the 2010-11 budget includes three Department of Parks and Recreation projects that are to be funded by private non-profits. In this case, the funds were not set-aside at the time of appropriation, which is why Provision 2 was added to state, "*The funds in this item shall not be expended without prior approval from the Department of Finance*."

As noted in the background section above, current statute contains checks and balances to prevent moving forward on the preliminary plans without the total required funding being deposited into the Endowment Fund. Further, current statute delineates a process whereby the subsequent phases of the Cemetery Project (i.e., working drawings and construction) will proceed only when funds are available as determined by the Director of Finance. This April letter is limited to the first phase – preliminary plans. Therefore, in considering this request, the Subcommittee may wish to modify the Administration's budget bill language to include a citation to the relevant statute.

Staff Recommendation: Approve the April letter with modified budget bill language citing the relevant Military and Veterans Code statute.

Vote:

Senate Budget and Fiscal Review—Mark Leno, Chair

SUBCOMMITTEE NO. 4 Agenda

Senator Michael J. Rubio, Chair
Senator Noreen Evans
Senator Doug LaMalfa

Thursday, May 5, 2011
9:30 a.m. or Upon Adjournment of Session
Room 112

Consultants: Brian Annis, Keely Bosler,
Kris Kuzmich, and Seija Virtanen

JANUARY BUDGET REQUESTS DENIED WITHOUT PREJUDICE AND APRIL FINANCE LETTERS

OUTCOMES

DEPARTMENTS TO BE HEARD

(Please See Detailed Agenda on Pages 2 and 3 for More Specific Listing and Order of Departments and Issues to Be Heard)

0502	California Technology Agency
0520	Secretary of Business, Transportation, and Housing Agency
0840	State Controller's Office
0845	Department of Insurance
0890	Secretary of State's Office
0971	California Alternative Energy and Advanced Transportation Authority
1110	Department of Consumer Affairs
1730	Franchise Tax Board
2320	Department of Real Estate
8380	Department of Personnel Administration
8880	Financial Information System for California (FI$Cal)
8955	California Department of Veterans Affairs

AGENDA – VOTE ONLY ITEMS

(Please see summary chart on Page 4)

AGENDA – DISCUSSION / VOTE ITEMS

Issues Proposed for Vote Only:

	Issue	Amount	Fund Source	Staff Recommendation
	Secretary of Business Transportation and Housing Agency (0520)			
1	Small Business Loan Guarantee Program Expansion	$84.4 million scheduled over three fiscal years.	Federal Funds	APPROVE, as specified
	State Controller's Office (0840)			
1	Increased Postage Expenses	$43,000 in 2010-11 $217,000 in 2011-12 and ongoing	Reimbursements	APPROVE
2	Transportation Audits Indirect Allocation Plans	$1,751,000 in 2011-12 and 12.6 two-year limited-term positions (Includes supplemental reporting language)	Reimbursements	APPROVE, as specified
	Department of Insurance (0845)			
1	Workers' Compensation Insurance Fraud Program: Local Assistance Workload Increases	$1,646,000 in 2011-12	Insurance Fund	APPROVE
	California Alternative Energy and Advanced Transportation Authority (0971)			
1	Energy Upgrade California Program	$205,000 in 2011-12	Reimbursements	APPROVE
	Department of Consumer Affairs (1110)			
1	Board of Professional Engineers and Land Surveyors Licensing Exams	$1,124,000 on a one-time basis	Special Funds	APPROVE
	Franchise Tax Board (1730)			
1	Data Security and Reliability: Enterprise Tape Library	Shift $2,290,000 from 2010-11 to 2011-12	General Fund	APPROVE
2	Voluntary Contribution Funding Codes: Budget Bill Clean-up	Language only	Language only	APPROVE
	Department of Real Estate (2320)			
1	SB 36 Mortgage Loan Originator Licensure (SAFE Act)	$216,000 in 2011-12 and 2 positions	Real Estate Fund	DENY
	Department of Personnel Administration (8380)			
1	Removal of Recruitment Contract Funding and Language	$350,000 in 2011-12 and modified budget bill language $350,000 in 2010-11 $350,000 in 2009-10	General Fund	APPROVE, as specified

Vote: Staff recommendation for all vote-only items adopted by 3-0 vote.

Issues Proposed for Vote Only – Issue Descriptions

SECRETARY OF BUSINESS, TRANSPORTATION, AND HOUSING AGENCY (0520)

Department Overview: The Secretary of the Business, Transportation and Housing Agency (BT&H Agency) is a member of the Governor's Cabinet and oversees 16 departments, including the following large departments:

- Alcoholic Beverage Control
- Corporations
- Housing and Community Development
- California Highway Patrol
- Motor Vehicles
- Financial Institutions
- Real Estate
- Managed Health Care
- Transportation

In addition, the Secretary's Office oversees programs, including the following, which are budgeted directly in the Secretary's Office:

- Infrastructure and Economic Development Bank
- Film Commission
- Small Business Loan Guarantee Program
- Tourism Commission

Budget Overview: The January Governor's Budget proposed total expenditures of $100.9 million ($4.2 million General Fund) and 60.7 positions for the Office of the Secretary – an increase of $78.2 million from the adjusted 2010-11 budget, and an increase of 1.5 funded positions. The primary reason for the year-over-year change is a one-time federal grant of $84.4 million to support the Small Business Loan Guarantee Program.

Current Budget Status: The Legislature made some modifications to the proposed budget for the Small Business Loan Guarantee Program, but otherwise approved the BT&H Agency budget as proposed. An April 1 Finance Letter was proposed to make some technical scheduling adjustments for federal grants to the Small Business Loan Guarantee Program which is discussed below as Issue 1.

Issue 1 –Small Business Loan Guarantee Program Expansion

April Letter Request. The Governor's April 1st Letter adjusts the budget to correctly reflect federal funds by year of receipt for the grants awarded to the Small Business Loan Guarantee Program. Instead of $84.4 million being received in 2011-12 (as was scheduled in the January Budget), the funds would be received as follows: $27.8 million in 2010-11, $27.8 million in 2011-12, and $28.7 million in 2012-13.

Background. The Governor's Budget requested various budget changes related to a federal grant award that will result in a one-time federal grant of $84.4 million for the Small Business Loan Guarantee Program (SBLG). This represents a significant expansion of the program which has typically had a trust-fund balance between $30 million and $40 million. The SBLG Program provides assistance to small businesses that may not qualify for traditional loans, by guaranteeing a portion of the loaned amount. The Administration requests to revert $20 million in General Fund support provided to the program one-time as part of the 2010 Budget Act (AB 1632, Chapter 731, Statutes of 2010). This reversion of $20 million is contingent on receipt of the federal funds. Finally, the Administration requests to double program staff from 1.5 positions to 3.0 positions.

Prior Subcommittee Action. The Subcommittee heard this item February 3 and February 10 and determined that the Federal grant will allow the State to expand this program, and at the same time realize a GF benefit of $20 million by reverting the augmentation provided last year. Specifically, the Subcommittee adopted the following:

a) The Governor's proposal to revert $20 million to the GF;
b) Budget Trailer Bill Language to direct that new loan guarantees use federal funds first;
c) Approved 0.5 new staff instead of 1.5 new staff;
d) Converted program administration funding to 50-percent GF and trust fund interest, and 50-percent federal funds, instead of eliminating all GF support for administration. This provided additional FDC administration funding over the base level for ramp-up, but still resulted in a GF expenditure savings; and,
e) Adopted provisional budget bill language to allow the Director of Finance to transfer up to $20 million from the GF to the Trust Fund, if loan defaults reduce the trust fund balance to the extent additional funds are necessary to maintain a 5:1 reserve ratio for outstanding loans. Joint Legislative Budget Committee (JLBC) notification would be required*.*

Staff Comment: To correctly reflect the installment appropriation for the $84.4 million grant, the Joint Legislative Budget Committee approved $27.8 million in federal expenditure authority for the Small Business Loan Guarantee Program in 2010-11 on March 25, 2011. The 30-day review period was waived so that the program would be positioned to meet the federal government's expectations for use of these funds.

The April 1st Letter proposes budget changes to correctly reflect the multi-year payment of the federal grant. The language would place $27.8 million into the Small Business Expansion Fund (consistent with federal regulations) for 2011-12.

This is recommended as vote-only because this is a technical fix, to correctly schedule the federal grant by fiscal year – there are no substantive changes to the proposal.

Staff Recommendation: Adopt the Administration's April 1st scheduling of federal funds, but maintain prior Subcommittee Action related to administrative costs and budget language.

STATE CONTROLLER'S OFFICE (0840)

For overview and budget information regarding the State Controller's Office (SCO), please see *page 33 of this agenda.*

Issue 1 – Increased Postage Expenses

April Letter Request. In an April Finance Letter, the Governor requests increased expenditure authority of $43,000 (reimbursements) in 2010-11 and $217,000 (reimbursements) in 2011-12 and ongoing, for increased postage expenses.

Background. The SCO is the chief financial officer of the state, whose responsibilities include mission critical functions such as general disbursements of payments and other mailings, which require postage. The cost of postage represents approximately 27 percent of the SCO's total ongoing 2011-12 Operating Expenses and Equipment budget. Actual postage costs for 2009-10 were $13 million and are budgeted at $14.2 million for 2010-11. As a result of the most recent United States Postal Service (USPS) rate increase, effective on April 17, 2011, the SCO estimates an increased cost of $61,000 in 2010-11 and $272,000 in 2011-12 and ongoing. Cognizant of the pressures on the GF, the SCO is requesting support for only the reimbursement share of the cost increase through this April letter.

Through an approved 2010-11 budget request, the SCO budget was augmented by $874,000 (various special funds) for projected increased costs in rent and an anticipated increase in postage costs; the total provided was split roughly evenly between the two cost areas. The postage increase did not occur. The SCO reports that the 2010-11 funds for the postage increase have not been spent and will instead be reverted at the end of this fiscal year.

Staff Comment. The SCO's 2010-11 budget was augmented by $442,000 for a postage increase that subsequently did not happen; as noted above, those funds have not been spent and will revert at the end of this fiscal year. On April 17, 2011, a postage increase was implemented.

Staff Recommendation. Approve the April letter.

Issue 2 – Transportation Audits Indirect Allocation Plans

April Letter Request. In an April Finance Letter, the Governor requests continuation of 12.6 positions and $1.751 million (reimbursements) on a two-year limited-term basis to authorize the Controller to continue providing audit services for Indirect Cost Allocation Plans (ICAPs) for Local Government Agencies (LGAs) on an interagency agreement with the California Department of Transportation (Caltrans).

Background. In the 2009-10 budget, the SCO received similar funding on a two-year limited term basis to provide, through an interagency agreement, audit services to Caltrans for audits of ICAPs for LGAs. This request would continue the ability of the SCO to provide these audit services to Caltrans. The ICAP audits are mandated by the Federal Highway Administration of LGAs that receive federal transportation funding. The purpose of an ICAP is to equitably allocate allowable indirect costs of an LGA to benefiting projects/cost objectives through an annual indirect rate. Audits of submitted ICAPs for the last two fiscal years have resulted in a reduction of indirect costs by more than $14 million per year due to discovery of errors and unallowable costs.

Staff Comment. On April 28, 2011, Senate Budget Subcommittee No. 2 on Resources, Environmental Protection, Energy and Transportation approved an April letter from Caltrans for the Caltrans side of this interagency agreement for audit services. The resources requested are limited-term, which is appropriate as the SCO indicates the federal audit requirements may change in future years. In approving this request, staff also recommends inclusion of Supplemental Reporting language to require the SCO report to the Legislature regarding federal audit requirements prior to the next fiscal year with a reporting date of March 1, 2012.

Staff Recommendation. Approve the April letter and supplemental reporting language.

DEPARTMENT OF INSURANCE (0845)

Department Overview. The California Department of Insurance (CDI) regulates the California insurance market and enforces the California Insurance Code, conducting examinations and investigations of insurance companies and producers and working to ensure the financial solvency of companies so that they will meet their obligations to policyholders and claimants. CDI investigates more than 300,000 complaints annually and responds to consumer inquiries. CDI also reviews and approves insurance rates to enforce the statutory requirement that rates are not excessive or unfair. CDI also administers the conservation and liquidation of insolvent and delinquent insurance companies and fights insurance fraud in conjunction with local and state law enforcement agencies.

Budget Overview. The January Governor's Budget provides CDI with 1,338 authorized positions and $224.94 million (Insurance Fund and reimbursements). This is an increase of 71 positions and $16.4 million.

Issue 1 – Workers' Compensation Insurance Fraud Program: Local Assistance Workload Increases

April Letter Request. In an April Finance Letter, the Governor requests increased expenditure authority of $1.646 million (Insurance Fund) local assistance in 2011-12 and ongoing to fund local District Attorney workers' compensation fraud investigation workload increases.

Background. The Workers' Compensation Fraud Program (WCFP) was established in 1991 (Chapter 116; Statutes of 1991), thereby making workers' compensation a felony, requiring employers to report suspected fraud, and establishing a mechanism for funding enforcement and prosecution activities. The Fraud Assessment Commission (FAC) was also established and mandated to annually determine the level of employer paid assessment necessary to fund investigation and prosecution of workers' compensation insurance fraud. Under law, this funding is restricted and cannot be used for any other purpose; after incidental expenses, at least 40 percent of the funds are provided to the DOI Fraud Division for enhanced investigative efforts, and at least 40 percent of the funds are distributed to local District Attorneys. At its September 8, 2010, meeting, the FAC approved an assessment of $31.874 million for local assistance, a 6.5 percent increase over 2010-11 funding. By approving this request, the expenditure authority for the District Attorneys' portion of the WCFP will be appropriately aligned with the current FAC assessment.

Staff Recommendation. Approve the April letter.

CALIFORNIA ALTERNATIVE ENERGY AND ADVANCED TRANSPORTATION AUTHORITY (0971)

For overview and budget information regarding the California Alternative Energy and Advanced Transportation Authority, please see page 31 of this agenda.

Issue 1 – Energy Upgrade California Program

Governor's Request: In an April 1 Finance Letter, the Administration requests an increase of $205,000 in reimbursements for CAEATFA to assist the California Energy Commission (CEC) by providing financial services for the Energy Upgrade California Program (EUC) which is funded by the federal American Recovery and Reinvestment Act (ARRA) of 2009. This request follows the Section 28 request submitted to the Department of Finance in the amount of $4.3 million for the current year.

Background: The CEC received $315 million through ARRA for energy-related projects and rebates. As part of this project CEC developed the EUC, a statewide energy and water efficiency and renewable energy generation retrofit program and contracted with the Local Government Commission (LGC) to run the program. LGC, in turn, has subcontracted with CAEATFA to provide financial services with respect to financial products and lending standards and financial subsidies.

The total amount of the program request is $4,523,000 ($4,318,000 in the current year pursuant to the Section 28 letter and $205,000 as a component of this BCP) through ARRA funding. The funds will be used for staff services, financial subsidy funds, trustee costs, financial advisor services, legal services, travel, and overhead.

This issue is suggested for vote only because the Joint Legislative Budget Committee approved the 2010-11 Section 28 letter for $4.3 million, which represents most of the program funding. The April Finance letter would conform to the JLBC action.

Staff Recommendation: Approve the April letter.

DEPARTMENT OF CONSUMER AFFAIRS (1110)

Departmental Overview and Mission. The Department of Consumer Affair's (DCA) Boards and Bureaus provide exams and licensing, enforcement, complaint mediation, education for consumers, and information on privacy concerns. DCA Boards and Bureaus establish minimal competency standards for more than 255 professions involving approximately 2.4 million professionals. There are currently 25 boards, a commission, three committees, and eight bureaus under the broad authority of the DCA.

Budget Overview. The Boards are budgeted under organizational code 1110, and the total proposed budget is $271.46 million (no GF) and 1,511.3 positions – an increase of $10.4 million and 35.6 positions over 2010-11.

The Bureaus are budgeted under organizational code 1111, and the total proposed budget is $231.34 million (no GF) and 1,386.6 positions – an increase of $14.2 million and 5.7 positions over 2010-11.

Issue 1 – Board of Professional Engineers and Land Surveyors Licensing Exams

April Letter Request. The Governor requests $1.124 million (one-time special funds) for the Board for Professional Engineers, Land Surveyors, and Geologists for fees to the National Council of Examiners for Engineering and Surveying to administer the national examinations to California applicants.

Board of Professional Engineers and Land Surveyors. The mission of the Board for Professional Engineers and Land Surveyors (BPELS) is to safeguard the life, health, property, and welfare of the public by regulating the practice of professional engineering and land surveying. In 2009, legislation was enacted that eliminated the Board for Geologists and Geophysicists and transferred all of the duties, powers, purposes, responsibilities, and jurisdiction to regulate the practices of geology and geophysics to the Board for Professional Engineers and Land Surveyors.

Licensing Exams. The California Business and Professions Code mandates the BPELS to receive applications for licensing, ensure that an exam for licensure is available and accepted in California, and ensure that each exam type is available at least once a year.

Currently, there are 16 different national exams and six state-specific exams for engineers, land surveyors, and geologists offered within California. The National Council of Examiners for Engineering and Surveying (NCEES) develops the national exams used by California. The national exams ensure that individuals licensed in California are accepted for license reciprocity in the other 39 states that use NCEES examinations and out-of-state applicants can gain licensure in California. The exams are administered by BPELS.

Security Breach. In April 2010, the BPELS found that an exam booklet was missing. The NCEES Board determined that the integrity of the exam process had been breached. The NCEES informed the BPELS that if California is to retain access to the national examinations, it must contract with NCEES to administer the examinations. BPELS has a financial liability for all compromised exams, and the amount of the liability varies by exam type. California's liability for the security breach is $2 million, and potential future liability is up to $7.6 million for all national engineering exams provided in California.

Cost of Providing Examinations. Currently, the BPELS administers 22 exams at a cost of approximately $2.45 million annually. This cost includes a $1.8 million contract with NCEES for the use of the NCEES exams. Once BPELS amends state regulations to allow for computerized testing, the contract funds to NCEES will be removed from the BPELS budget, thus saving the state funds in the long-term. After the computerized testing is allowed for, the payment NCEES will receive for administering the exams will come directly from the licensed population in the form of exam fees.

In 2011-12, the one-time funds will pay additional fees to NCEES to administer the exams, while BPELS amends state regulations to allow for a computer-based testing format and lowers the state licensing fees. Additionally, by having NCEES administer the exams, California is released from liability for exam security breaches.

Staff Recommendation. Approve the April letter.

FRANCHISE TAX BOARD (1730)

For overview information regarding the Franchise Tax Board (FTB), please see page 22 of this agenda.

Issue 1 – Data Security and Reliability: Enterprise Tape Library

April Letter Request. The Governor requests shifting $2.29 million approved last year to replace FTB's Enterprise Tape Library from the current year to 2011-12. The expenditure of these funds has been delayed and this proposal would better align the funding to the correct fiscal year. The April Finance Letter is also requesting $2.27 million in 2012-13 to complete the replacement. This delay in expending these funds has not impacted the project costs or the final completion date of the project.

Background. Data security and reliability is critical for FTB given the volume of confidential taxpayer data it maintains. The FTB has employed a defense-in-depth strategy to protect this information where multiple layers of defense are placed throughout its information technology system so that if one fails there are others layers that prevent against a security attack.

Furthermore, the FTB's data reliability is being threatened by outdated equipment and software that is out-of-support. For example, the FTB's Enterprise Tape Library System, which is critical to providing continuous access to the up-to-date accurate information that FTB's automated systems rely on, is at risk of failure. If this system failed, FTB's productivity could be severely hampered and data security could be compromised.

Staff Recommendation. Approve the April letter.

Issue 2 – Voluntary Contribution Funding Codes – Budget Bill Clean-Up

April Letter Request. The April Letter includes amendments to the budget bill to add four new funds and delete four funds that did not meet the voluntary contribution limits required to remain on the state tax return. The four additions that were established by Statutes in 2010 include the following:

- Arts Council Fund
- California Police Activities League (CALPAL) Fund
- California Veterans Home Fund
- Safely Surrendered Baby Fund

The four funds that did not reach the $250,000 threshold for contributions and are proposed to be eliminated include the following:

- ALS/Lou Gehrig's Disease Research Fund
- California Military Family Relief Fund
- California Ovarian Cancer Fund
- Municipal Shelter Spay and Neuter Fund

Background. Current law allows taxpayers to contribute amounts in excess of their tax liability to various voluntary contribution funds listed on the state tax return by checking a box on their California income tax form. These funds must reach the minimum level of $250,000 in their second taxable year. If they do not meet the $250,000 minimum, the law authorizing these fund designations is repealed.

Staff Comments. This proposal is strictly limited to adjusting the budget bill to properly align existing law with the budget bill. The underlying statutes authorizing the voluntary contribution funds are automatically repealed when the minimum threshold is not met.

Staff Recommendation. Approve the April letter.

DEPARTMENT OF REAL ESTATE (2320)

For overview information regarding the Department of Real Estate (DRE), please see page 37 of this agenda.

Issue 1 – SB 36 Mortgage Loan Originator Licensure (SAFE Act)

Governor's Budget Request. The Governor requests $216,000 (Real Estate Fund) and two positions for continued implementation of the federally mandated Secure and Fair Enforcement Licensing Act of 2008 (SAFE Act) which requires states to implement a new licensing program for mortgage loan originators (MLOs).

2010-11 Budget. The 2010-11 budget included $2.8 million (Real Estate Fund) and 27 positions to begin implementation of the SAFE Act.

Prior Subcommittee Action. This request was denied without prejudice at the Subcommittee's January 25, 2011, hearing so that all factors and the DRE's resources could be considered at one time (it was indicated to staff that the DRE might have additional requests related to SAFE Act implementation during Spring budget hearings). Further, the Senate Business and Professions Committee held an oversight hearing on February 28, 2011, focused on DRE enforcement and consumer protection issues. The DRE now reports that there are no additional requests forthcoming with the exception of Issue 1 on page 37 of this agenda, an April Finance Letter related to the relocation and consolidation of the DRE's Headquarters and Examination Center.

Background. The federally mandated SAFE Act requires all states to license and register their MLOs through a nationwide registry called the National Mortgage Licensing System (NMLS). Chapter 160, Statutes of 2009 (SB 36), brought California into compliance with the SAFE Act by requiring those engaging in MLO activities to obtain a license from the Department of Corporations or, if a real estate licensee, obtain a license endorsement from the DRE.

At this point in the SAFE Act implementation process, the main drivers of the additional licensing and enforcement workload for the DRE was the MLO notification in 2010 and ongoing license endorsement renewal process and the annual Business Activities Report and Call Report requirements for all MLO brokers, respectively. With regard to enforcement activities, the workload will be driven by the number of NMLS registrants required to file the mandated reports and the timing of the submission of those reports. More specifically, the Business Activities Reports are first due on a rolling basis beginning on January 2, 2012 (the reports have to be submitted within 90 days after the end of the broker's first fiscal year; April 2, 2012, is the final date these first reports could be filed with the DRE to meet the 90-day requirement). The Call Reports are required to be submitted on a quarterly basis beginning May 15, 2011.

Staff Comment. In approving SB 36, the Legislature approached SAFE Act compliance in a narrow sense by requiring a new endorsement on existing real estate licenses. Licensees pay a $300 fee for that endorsement. Staff notes that while this approach has resulted in the least disruption to existing systems and minimized compliance costs to both the state and licensees, the SAFE Act has represented, and will continue to represent, new workload for DRE. However, due to the timeline when SAFE Act enforcement activities will commence in earnest, the actual workload data is still relatively unknown. Additionally, the DRE has indicated that it is exploring available business analytic technology opportunities to substantially reduce the number of positions needed to review the required reports. The Administration has confirmed that the approach is for the DRE to submit a new comprehensive SAFE Act-related request in a future budget cycle rather than taking a fragmented approach, such as that contained in this request.

Staff Recommendation: Deny the request.

DEPARTMENT OF PERSONNEL ADMINISTRATION (8380)

Department Overview. The Department of Personnel Administration (DPA) is the Governor's chief personnel policy advisor. DPA represents the Governor as the "employer" in all matters concerning state employer-employee relations. DPA is responsible for all issues related to salaries, benefits, and position classification. For rank and file employees, these matters are determined through the collective bargaining process; for excluded employees, these matters are determined through a meet and confer process.

Budget Overview. The January Governor's Budget provides the DPA with 246 authorized positions and $86.4 million ($9.3 million GF). This is an increase of zero positions and $625,000.

Issue 1 – Removal of Recruitment Contract Funding and Language

April Letter Request. In an April Finance Letter, the Governor requests a reduction of $350,000 GF in 2011-12 and removal of provisional budget bill language to reflect the fiscal year 2008-09 expiration of recruitment contracts for medical professionals.

Background. In the 2007-08 Budget, the Legislature approved on a two-year limited-term basis an augmentation of $350,000 GF and provisional budget bill language for recruitment contracts for medical professionals. The funding and language should have been removed in the 2009-10 Budget when the limited-term period expired. For unknown reasons, this action was not taken; therefore, the funding and provisional language remained in DPA's budget.

Staff Comment. According the DPA, the $350,000 GF was not expended in 2009-10 and the DPA reports that it has not and does not intend to spend those funds. However, the DPA does have the ability to still liquidate the funds should they chose to since departments have one year to encumber and two years to liquidate. The 2009-10 funds in question, therefore, could "last" until the end of 2011-12.

With regard to the $350,000 GF contained in the 2010-11 budget, the DPA reports that the funds have also not been expended. Therefore, in its consideration of this request, the Subcommittee may wish to consider adopting budget bill language to revert the 2010-11 funds, as well as the 2009-10 funds, thereby ensuring that the DPA no longer has the ability to access these funds, for additional savings of $700,000 GF.

Staff Recommendation: Approve the April letter to delete the provisional budget bill language and reduce DPA's budget by $350,000 GF in 2011-12; additionally, adopt new reversion items in the 2011-12 budget to realize an additional $700,000 GF savings combined from 2009-10 and 2010-11.

INFORMATION TECHNOLOGY

Issues Proposed for Discussion / Vote

Issue 1 – California Technology Agency (0502) 2009 Governor's Reorganization Plan No. 1

Background. On May 10, 2009, the Governor's Reorganization Plan No. 1 (GRP) took effect thereby beginning the process of consolidating statewide information technology (IT) functions under the California Technology Agency (formerly the Office of the State Chief Information Officer, or OCIO). Since that time, the primary strategic objective has been to transform state government to become more responsive to Californians' needs and to operate more efficiently and transparently through the use of technology.

As required by statute, each year the California Technology Agency (Technology Agency) has updated the state's IT Strategic Plan (first adopted in 2009). The 2011 Statewide IT Strategic Plan streamlines and further clarifies the strategies articulated in the 2009 and 2010 Strategic Plans, and contains the following three strategic goals: (1) Make Government Transparent, Accessible, and Secure; (2) Drive Innovation and Collaboration; and (3) Make Information Technology Reliable and Sustainable Through Consolidated Platforms and Shared Services. In short, and through the implementation of the GRP, the California Technology Agency (Technology Agency) seeks to consolidate the state's IT infrastructure while laying the groundwork for more robust and more sustainable platforms, improve project management practices, oversight, and training, and create an architectural framework to reduce redundancy and improve operations.

Current statute also requires the Technology Agency to produce an annual IT performance report consisting of a variety of assessments and measurements, including the progress made in enhancing IT human capital management, improving the IT procurement process, and enhancing the security, reliability, and quality of IT networks, services, and systems. The Technology Agency is also required to post these performance targets and progress towards these targets to its public internet web site. Finally, current statute requires the Technology Agency to report, at least annually, to the Director of Finance cost savings achieved through improvements to the way the state acquires, develops, implements, manages, and operates state technology assets, infrastructure, and systems.

Chapter 404, Statutes of 2010 (AB 2408) codified the GRP and defined targets and timelines for IT consolidation across the executive branch, including modernizing the state's IT infrastructure to increase efficiency, reduce energy usage, and save costs. With the Technology Agency taking the lead, departments are now required to meet the following mandates: (1) achieve a 20 percent reduction in energy usage by July 2011, and 30 percent by July 2012; (2) achieve a 50 percent reduction in data center raised floor space by July 2011; (3) transition mission-critical and public-facing applications to Tier III data centers and close all other existing server rooms by June 2013; (4) begin migrating from existing network services to the California Government Network no later than July 2011; and (5) begin migrating to the state's shared e-mail solution no later than June 2011.

Chapter 404 also made changes to the IT procurement process to coordinate IT resources across the executive branch. Effective January 1, 2011, departments and agencies are now required to submit IT solicitations (Requests for Proposal) valued at more than $1 million to the Technology Agency and the Department of General Services prior to releasing to the public. Prior to this statutory change, the Technology Agency was not formally included in the IT solicitation process.

Staff Comment. Prior to the adoption of the GRP, state IT had been largely decentralized for years. The GRP, therefore, represented a new and substantial change of course. Since its approval in 2009, Subcommittee No. 4 has annually "checked-in" on the status of its implementation. In those hearings, the Subcommittee focused on examining how IT functions and resources have been streamlined, how statewide IT policies have been standardized, the status of efforts to meet the performance metrics contained in the GRP, and the savings achieved (or to be achieved). All of these areas are valid and the Technology Agency has made great strides in achieving the goals of the GRP; these areas are all also largely captured within existing reports, such as the annual IT strategic plan or other statutorily-required reporting mechanisms. Therefore, as we near the two year anniversary of the adoption of the GRP, and cognizant of the fact that the implementation of the GRP is and will continue to be an evolving process, staff recommends today's discussion focus on what further improvements are needed to what information related to the implementation is collected and how that information is reported and shared to ensure that a complete picture of the implementation is provided on an ongoing basis.

Staff notes that one of the challenges to date with the story of the GRP is that a particular focus has been placed on savings. This is understandable, especially in light of the state's fiscal condition, but it is important to acknowledge that the GRP resulted in some new upfront costs in the early years with likely greater out year savings. This fact likely offset some of the immediate achieved savings. Additionally, capturing IT savings is a challenge as day-to-day IT expenditures are not a defined budget expenditure. Rather, IT expenditures are largely included in departmental Operating Expenses and Equipment funds (and paid to the Technology Agency through rates charged for products and services provided) which makes it difficult to have effective expenditure control mechanisms.

As identified below, it is clear that the Technology Agency is making strides to generate savings though reduced data center square footage, improved energy usage, and decreased server usage, but capturing that savings is difficult (primary reason why savings through a control section is unsuccessful). For example, reducing the data center square footage and the number of servers housed at the data center may result in decreased rates charged by the Technology Agency, but increased storage capacity, staff costs, or usage requests may result in increased rates charged. In this example, if a 3-cent rate decrease is offset by a 3-cent rate increase, the client department sees no change in costs; savings are not captured, but we know the job is being done more efficiently.

This singular focus on savings also misses other key and valid parts of the story where successes have been achieved but have not been reported. For instance, another outcome of the GRP that has proven difficult to quantify are the costs (and risks) that have been avoided in the past two years. The Technology Agency has provided information to staff indicating that, since it was established in 2008 (formerly the OCIO), the state has achieved more than $800 million in savings and cost avoidances through numerous technology initiatives including state-wide IT consolidation, IT Project Oversight, IT Capital Plans, IT Acquisition Plans, annual IT Cost Reporting, and contract renegotiations. Examples of those savings/avoidances include:

- Reduced data center square footage by more than 100,000 square feet. The space savings alleviated the need for a new data center facility, eliminating more than $40 million in capital costs and $24 million in annual operating expenses.
- Identified more than $693 million in cost avoidance through the IT Capital Planning process.
- Reduced IT consultant contracts by $17 million and IT project costs by $52 million through the IT Acquisition Planning process.
- Renegotiated the CalNet 2 contract reducing telecommunications costs to state agencies by $25 million annually.
- Conducted an assessment of wireless rates resulting in more than $3 million in savings to state agencies.
- Reduced data center rates charged to state agencies by $23.94 million:
  - $8 million in rate reductions due to network consolidation.
  - Storage rates have gone down by more than 90 percent since 2008 (from $24 per gigabyte per month to $2 per gigabyte per month).

However, this information on cost (and risk) avoidance is not currently widely reported or shared. Therefore, staff recommends the Subcommittee consider adopting both budget trailer bill and supplemental report placeholder language to improve upon existing reporting metrics to capture these types of additional elements of the GRP implementation efforts. Developed collaboratively with the LAO, Technology Agency, and DOF, the additional metrics would include: (1) reporting on cost (and risk) avoidance and (2) any potential impairments that have been identified to the continued successful implementation of the GRP. Additionally, staff recommends that through the adoption of additional placeholder supplemental reporting language a process be established to convene an annual meeting on the overall status of the implementation of the GRP, and more specifically on lessons learned to date and what barriers to success have been identified. Finally, staff recommends that a copy of the annual report on IT savings also include cost avoidances and that report be transmitted to the Joint Legislative Budget Committee and fiscal committees of both houses of the Legislature.

As the Subcommittee considers these issues, it may wish the Technology Agency and Administration to respond to the following questions:

1. The Technology Agency has identified more than $693 million in cost avoidance through the IT Capital Planning process. What specific examples can the Technology Agency share with the Subcommittee to better delineate these savings? Are there examples of IT projects that were denied? Can the Technology Agency point to an example where the efforts of two departments pursuing similar projects were combined, thereby achieving some measure of economies of scale?
2. One of the functions consolidated in GRP 1 was "human capital management." Could the Technology Agency briefly describe the changes that have been implemented with regard to IT human capital?
3. How has the Technology Agency addressed IT project management in the past year? How has the Technology Agency used project management resources to address projects like 21st Century and FI$Cal (Issue 4 below), which are in process?
4. Savings are either one-time or ongoing. For the savings achieved to date, what percentage is one-time versus ongoing? How will that ratio change over time?

Staff Recommendation: Approve placeholder budget trailer bill language and supplemental report language to improve reporting and information sharing related to the implementation of the GRP.

Vote: Staff recommendation approved by 3-0 vote.

Issue 2 – California Technology Agency (0502) Independent Project Oversight

Governor's Budget Request. The Governor requests $966,000 (Technology Services Revolving Fund) and nine permanent positions for Independent Information Technology Project Oversight (IPO) in 2011-12 and ongoing to meet workload increases and mandated responsibilities of Chapters 183 and 404, Statutes of 2007 (SB 90) and Statutes of 2010 (AB 2408), respectively, and to ensure consistent project implementation of the state's IT projects.

Prior Subcommittee Action. This request was denied without prejudice at the Subcommittee's February 7, 2011, hearing, so that all factors and the Technology Agency's (Technology Agency) resources could be considered at one time (it was indicated to staff that the Technology Agency might have additional related requests during Spring budget hearings). The Technology Agency reports that there are no additional requests forthcoming.

Background. The increased expenditure authority in this request is for a staffing expansion that the Technology Agency considers a critical priority due to legislative mandates, increased public visibility, and the need to ensure consistent project implementation of the state's IT projects. These positions would provide independent project management services to customer departments. These positions are also consistent with the GRP, and its goals of enhancing IT human capital management. The costs associated with the IT project management will be funded by the agency or department administering the project; the Technology Agency would be reimbursed 100 percent by the department or agency requesting the services. Once the Technology Agency has created a professional state governmental entity, comprised of state staff, to manage and direct IT policy, standards, and projects, the state's current reliance on high paid contractors will be diminished. The state currently spends approximately $17.2 million annually on contracted IT project oversight and management.

Staff Comment. The proposed positions represent the beginning of the implementation of the Technology Agency's expanded role as outlined in Chapter 404. Staff concurs that having IPO conducted in-house (as opposed to contracted out) will save the state as the state will eventually no longer rely on highly paid contractors and will instead have developed a cadre of IT professionals within state service.

Staff Recommendation: Approve the request.

Vote: Request approved by 3-0 vote.

Issue 3 – Franchise Tax Board (1730) Enterprise Data to Revenue Project

Background. The Franchise Tax Board (FTB) is one of the state's two major tax collection agencies. The FTB's primary responsibility is to administer corporation tax programs and California's personal income tax (PIT). In addition, FTB administers several non-tax-related programs, including the collection of child support payments and other court-ordered payments. The FTB is governed by a three-member board, consisting of the Director of Finance, the Chair of the Board of Equalization (BOE), and the State Controller. An executive officer, appointed by the board, administers the daily operations and functions of FTB.

The Conference Report (SB 69, Budget) passed by the Legislature on March 17, 2011, contains $547.9 million General Fund to support FTB's operations.

The number of personnel-years (PYs) for FTB is budgeted to decline slightly from 5,434 to 5,260.

Tax Gap Reduction Measures

Summary. The FTB estimates that its total tax gap is about **$6.5 billion**. The tax gap is defined as the total tax receipts due to the state less the tax receipts collected by FTB. The department has undertaken several initiatives over the last six years to reduce this tax gap using an enterprise approach. An enterprise approach means that staffs from all different divisions at FTB are involved in reducing the tax gap, including filing, audit, legal, and collections divisions.

1. Enterprise Data to Revenue Project

Background. The FTB's tax filing system has not been substantially updated in the last 25 years. In order to modernize the FTB's filing system, the board initiated the Enterprise Data to Revenue (EDR) Project two years ago. This project will introduce a new PIT and Business Entity return processing system including expanded imaging, data capture, and return validation. Annually, the FTB processes approximately 15 million PIT returns and one million Business Entity returns.

Overall, this project will enable FTB to correct erroneous returns in a timelier manner. It will also be more effective at providing data to identify noncompliance patterns and help identify fraudulent activity. This data system will also allow FTB to better prioritize its workload based on highest cost recovery. The FTB indicates that the new system will also expand self-help tools for taxpayers and tax practitioners to improve the filing and payment activities.

The FTB is using an alternate type of procurement for the EDR project that invites bidders to propose a comprehensive solution to address the overall goals outlined by the EDR project, instead of dictating the solution to the bidders. In this type of procurement, the State enters into a contract with a **Primary Solution Provider (PSP)** and the State works collaboratively with the provider to find a solution that meets the goals of the State. The FTB received proposals last year and chose a PSP in November 2010.

The FTB is also using a **benefits based procurement model** to acquire the EDR Project and get the best value and business driven solution. This model is based on acquiring innovative solutions to strategic business problems and only compensating the contractor when these solutions deliver new tax revenues and after certain State costs are recouped. Revenue benefits are then shared with the contractor up to a fixed contract amount. Furthermore, the contract is constructed so that the State does not incur upfront expenses to compensate the contractor.

When fully implemented, the FTB estimates that the EDR project will bring in over **$1 billion in ongoing revenue annually**. This will help to address the $6.5 billion annual tax gap through increased collection of tax revenues that are due to the State but currently unpaid or uncollected for various reasons. Overall, the **one-time costs of the PSP contract are estimated to be $398.9 million** over the life of the 66-month (5.5 year) contract. This is significantly more than earlier anticipated costs of the project ($234 million). However, the State is now estimating that the proposed solution by the vendor will generate approximately $1 billion more in revenues over the life of the project.

Finance Letter. The Governor's April 1 Finance Letter requests $28.9 million General Fund to support the EDR project in the budget year. Last year, the Legislature approved a $10.2 million request, including 72 new positions. These costs will be more than offset by the additional revenues that the FTB estimates will be received in the 2011-12 fiscal year. The FTB anticipates generating $65.3 million in additional revenues in 2011-12 which is nearly $40 million more than initially anticipated prior to the FTB receiving the PSP solution.

Specifically, the funding requested in the budget year supports the following expenditures:

1. **Personal Services.** Includes $3.9 million for support of personal services. However, no additional positions are provided in this budget proposal. The department has indicated that it will redirect existing vacant positions to support this proposal in the short term.
2. **PSP Contract.** Initial compensation benefits ($25 million) to the PSP paid from additional revenues collected due to the implementation of several "early win" deliverables that will result in additional revenues in the first two to 18 months. Some of the early win deliverables are business process changes that do not require the entire information technology solution to be in place, including making changes to the tax forms to adjust for common mistakes related to real estate deductions and adding additional fields of data to the Accounts Receivable Collection System database.
3. **Independent Verification and Validation (IV&V) Contract.** Funding ($1.3 million) to acquire an IV&V contractor which is a standard practice of the State when entering into contracts for large information technology projects.
4. **Cost Reasonableness Contract.** Funding ($110,000) for Cost Reasonableness consultant services. This consultant will act as another check and balance on the main PSP contract to ensure that the costs charged to the State in delivering the project are reasonable and not outside the normal industry standards.

Staff Comments. Overall, staff finds that the EDR project has been thoroughly planned and the FTB has obviously done significant work to ready the organization for the implementation of the new system, including a complete documentation of their business processes. However, the proposed solution by the PSP has a considerably different cost and revenue structure than originally estimated. It will be critical that the state monitor how the estimated cost and revenue structure of this project tracks with actual revenues and expenditures. Furthermore, the calculation of the revenues attributable to the EDR project is essential to evaluating the relative value of the PSP contract.

- **FTB.** Can you please describe the process you are putting in place to measure what revenues benefits are attributable to the EDR project?
- **FTB.** How will major amendments to the PSP contract be handled if outcomes turn out to be different than estimated?

The Finance Letter assumes that a Section 11 is submitted in the current fiscal year to allow the state to enter into the contract with the PSP. This has not been received.

- **DOF.** What is the status of the Section 11 request for the current year?

Overall success in implementing a new information technology solution requires careful planning and training so that the users interfacing with the system can be successful in transitioning to the new system.

- **FTB.** What steps has FTB put in place to build in redundancy in the system in order to improve outcomes and ensure a smooth transition?
- **FTB.** What steps has FTB taken to ensure adequate training for the workforce transitioning to the new system?

The FTB received authority to hire 72 additional positions to support the EDR project last year. Staff understands that they need to fill an additional 52 positions to support the EDR project in the budget year for a total of 124 positions. The FTB has not received authority to hire 52 new positions in the budget year and is planning to redirect vacant positions internally to address the EDR workload. The April Finance Letter includes $3.9 million General Fund to support these redirected positions because these redirections would bring FTB's vacancy rate below 5 percent. (It is standard state budgeting practice to assume 5 percent [salary] savings when funding positions.) The FTB indicates that the redirection can be managed in the interim, but staff finds that the ongoing success of the project could be jeopardized if the implementation of the EDR solution is significantly under resourced – potentially leading to a pennywise pound foolish result. Furthermore, other revenue generating aspects of FTB's operations could be negatively impacted by the redirection.

- **FTB.** What are the main categories of staff needed to implement the EDR solution?
- **FTB.** Will these redirections have an impact on FTB's operations?

Staff Recommendation. Hold this issue open pending receipt of the 2010-11 Section 11 request.

Item held open.

Issue 4 – Financial Information System for California (FI$Cal) (8880) Budget Request for 2011-12

Department Overview: The Financial Information System for California (FI$Cal), is an Enterprise Resource Planning (ERP) information technology (IT) project intended to replace, consolidate, and upgrade multiple legacy financial systems with a single system that would encompass the areas of: budgeting; accounting; procurement; cash management; and financial management. The development of FI$Cal resides with four "Partner Agencies": the Department of Finance, the State Treasurer's Office, the State Controller's Office, and the Department of General Services. The FI$Cal system will be implemented in several phases, or "waves," over the next decade. Budget Control Section 8.88 is a technical fiscal provision that directs special funds to the FI$Cal project and it will be made to conform to the final budget adopted under the 8880 budget items.

January Budget Overview: The January Governor's budget proposed $70.8 million ($20.9 million GF) for continuing the FI$Cal project. This represents a year-over-year increase of $29.0 million ($5.2 million GF). Funded positions would grow from 62.1 to 95.9. The reason for the funding increase is that the project would be moving into the implementation stage with contract award to the vendor by December 31, 2011. The 12-year cost of fully implementing the project is estimated at $1.6 billion (both GF and other funds). The Administration is exploring financing options such as bonding and vendor-financing to spread costs over a longer period.

Current Budget Status: In February, the Subcommittee maintained the funding level proposed by the Governor, but indicated the FI$Cal budget would be reviewed further and heard again in the spring. The Subcommittee expressed concern about the GF cost of the FI$Cal project given the budget shortfall.

Governor's Revised Budget Request: The Administration has issued a Spring Finance Letter that redefines the budget year request for the FI$Cal project to reduce costs in 2011-12 and reflect the new project schedule. The new request reduces the requested funding for the budget year by $32.4 million ($18.4 million GF), and pushes the project schedule back by about 4 months. The revised budget proposed for 2011-12 is $38.5 million ($2.5 million GF). The request for 33 new positions made in January, would also be withdrawn.

Project Timeline: Currently, three selected vendors are completing the "Fit-Gap," or stage I contract, which involves a review of potential gaps between the vendor's software and the state's business requirements. Project staff have also asked the three vendors to propose financing options and have held discussions with the State Infrastructure Bank (I-Bank) on financing options. The following are key upcoming dates, as revised in the April Finance Letter:

- **June 2011** – Proposals due from the competing vendors.
- **January 2012** – Submission of Report to the legislation outlining the proposed vendor and IT solution.
- **April 2012** – Award of system contract (contingent on legislative support).

Project Financing: The FI$Cal project has produced a white paper on funding options. The paper outlines the following three options for financing the FI$Cal project:

- **Pay-Go**: Fund project costs in the budget as these costs are incurred, which results in the lowest overall project costs, but requires huge up-front costs in 2012-13 to 2017-18;
- **Vendor Financing**: Some of the contract costs would be financed through the vendor to help reduce the initial costs and spread out the costs over an additional five years; and,
- **I-Bank/Bond Financing**: Provides the lowest up-front costs, but has the highest overall costs by spreading costs over 15 years.

Staff Comments: The FI$Cal project is a multi-year effort which is completing its third year as a stand-alone budget item. Fiscal year 2011-12 is a pivotal fourth year for the project, in which the Administration will select a preferred product and partner, as well as a financing plan. The Administration will present the proposal to the Legislature for their review in the winter and spring of 2012. To the degree the solution proposed next year has the Legislature's support, the fiscal cost in 2012-13 can be managed through defining the speed of the roll-out and the financing strategy.

Staff Recommendation: Approve the FI$Cal budget as modified by the April Finance Letter.

Vote: Staff recommendation approved by 3-0 vote.

Issue 5 – Secretary of State (0890) California Business Connect Project: Phase I

April Letter Request. In an April Finance Letter, the Governor requests one-time increased expenditure authority of $1.16 million (Reimbursements) for Phase I of the California Business Connect Project, scheduled to begin in July 2011 with a projected completion date of June 2016.

Prior Budget Actions. Initially funded in 2001, with total project costs of $33.6 million (roughly $31.6 Business Fees Fund with remainder from the Business Reinvestment Fund) the Legislature approved the SOS's Business Automation (BPA) Project, which was expected to automate and modernize business processes. The BPA was approved for two phases, with Uniform Commercial Code (UCC) filings and other lien-related filings as the first phase and Business Entities, Special Filings, and Trademarks as the second phase. The BPA resulted in the customization and modification of a commercial-off-the-shelf product to support the statutory and business requirements for UCC and other lien-related filings. After the UCC phase was implemented in 2006, the vendor notified the SOS that their business model had changed; therefore, the BPA scope was reduced to the first phase only. As of January 1, 2010, the BPA vendor no longer provides maintenance and operational support for the UCC system; replacement of this system is scheduled in the final phase of the Business Connect project.

The 2010-11 budget included $1 million (Business Fees Fund) over two years to reduce the current backlog of Business Entity Filings and Statements of Information applications in the Business Programs Division. Of the $500,000 available under each year of the plan, $250,000 is for short-term information technology (IT) improvements to increase the functionality of the current electronic filing system and $250,000 is for staffing costs. When this two-year plan was adopted, the SOS indicated that it was intended to dovetail into a future IT project which would serve as the long-term solution to automate the Business Program Division.

Background. The SOS is responsible for the administration and enforcement of laws pertaining to filing documents associated with corporations, limited partnerships, and perfecting security agreements. On an annual basis, the SOS' Business Program Division (BPD) receives over a million business filings and requests a year. These filings by businesses are statutorily required and are not effective until reviewed and filed by the SOS. The filings and requests are comprised generally of two categories: (1) Business Filings, required of corporations, limited liability companies, and limited partnerships, which include such documents as articles of incorporation, trademarks, and other special filings; and (2) Statements of Information, which are required on an annual basis for corporations and on a biennial basis for limited liability companies, and also include common interest development association statements and publicly traded disclosure statements. Business filers are currently charged from $15-$150 dependent on the type of filing. Businesses can also pay additional fees to receive expedited service, such as $350 for 24-hour turnaround or $750 for same-day service.

The current process for accounting for and accepting these filings and requests is labor-intensive and reliant on several antiquated legacy computer systems, as well as a "paper" database (index cards) system. The SOS utilizes 23 separate Information Technology systems to support 15 of the filing types; the remaining eight filing types are essentially paper-based manual systems supported only with basic automation tools, such as Microsoft Word and Excel.

In May of 2009, the BPD had a backlog of 4,752 Business Filings with a 22-calendar day wait time; Statements of Information had a backlog of 36,737 filings with a 15-calendar day wait time. After the 2009 budget line-item veto which represented a 10 percent reduction to all constitutional offices including the SOS, and in May 2010, the Business Filings backlog had increased to 30,093 with a 72-calendar day wait time; the Statements of Information backlog had increased to 89,322 with a 52-calendar day wait time. In October of 2010, the backlogs had grown to 117-calendar days for Business Filings and 101-calendar days for Statements of Information.

As noted above, as part of the 2010-11 budget, a $1 million two-year plan was adopted to reduce the current backlogs in the BPD. As of April 11, 2011, the SOS reports that $300,000 has been spent, resulting in the processing of 94,000 Business Filings with $2.8 million in filing fees attached. This activity reduced the Business Filings backlog by over six weeks (from 117-calendar days to 72-calendar days). The funding was utilized to keep the backlog in Statements of Information relatively flat (the backlog in October 2010 was 101-calendar days; the April 2011 backlog is 111-calendar days). Progress was not made in reducing this backlog because the annual volume of filings is so large.

As of April 11, 2011, the current BPD backlog totals 200,000 documents waiting to be processed; of these, roughly 70,000 are Business Filings, with the remainder Annual Statements of Information. The SOS estimates that $3 million in uncashed checks are attached to these filings. Depending on type of filing, the current wait time is from two to four months.

The Business Connect Project is proposed as a business- or solutions-based procurement whereby vendors are provided with a business case and fundamental requirements which they then propose and submit solutions to meet the SOS' needs. Phase 1 consists of the development of the SOS' business and functional requirements which becomes the Request for Proposal (RFP) that vendors then respond to. More details about the technical solution, including a more robust estimate of project costs, will be outlined in a Special Project Report (SPR) to be filed with the California Technology Agency after vendor responses to the RFP are received. Based on the approved SPR, additional spending authority for each subsequent phase of the project will be sought from the Legislature. The SOS estimates total project costs of $23.7 million. The fund source is fees currently paid by businesses for filings and services.

Since 2006-07 and through 2009-10, both Reimbursements (expedited and special handling fees) and Business Fees Revenues (standard filing fees) have represented a GF solution totaling $23.1 million and 40.7 million, respectively. In 2010-11, it is estimated that $9.2 million in Reimbursements and $1.1 million in Business Fees Revenues will transfer to the GF. In 2011-12, it is projected that $9.0 million in Reimbursements and $432,000 in Business Fees Revenues will transfer to the GF. Figures 1 and 2 below provide further detail as to these collections and GF transfers.

Figure 1
Reimbursements Collected and Transferred to the GF (dollars in thousands)

	2006/07	2007/08	2008/09	2009/10	*2010/11 Estimated*	*2011/12 Projected*
Revenues	$13.4	$13.0	$11.4	$14.0	*$16.2*	*$16.2*
Expenditures	$7.3	$7.3	$7.3	$6.8	*$7.0*	*$7.2*
Total Excess Transferred to GF	$6.1	$5.7	$4.1	$7.2	*$9.2*	*$9.0*

Figure 2
Business Fees Fund Revenues Collected and Transferred to the GF (dollars in thousands)

	2006/07	2007/08	2008/09	2009/10	*2010/11 Estimated*	*2011/12 Projected*
Revenues	$51.0	$47.0	$44.4	$38.9	*$39.5*	*$39.5*
Expenditures	$32.4	$36.3	$35.8	$36.1	*$38.4*	*$39.1*
Total Excess Transferred to GF	$18.6	$10.7	$8.6	$2.8	*$1.1*	*$.4*

Staff Comment. The Business Connect Project has merit. The existing process is inefficient, the current legacy systems present a challenge to operate and maintain, and that the current backlog does not help the state's business climate. While the fees businesses have been paying have represented a GF solution in recent years, these fees were not paid with that intent. The SOS also estimates that the Business Connect Project, when complete, will save the state $5.6 million per year which means the costs of the project could be recouped in a fairly expedient manner.

Staff notes, however, two concerns with the proposed project. First, with regard to the fund source, as noted above the primary funding source for this project are the expedited fees paid by businesses. While a relatively stable revenue source in recent years, the majority of this revenue can be directly correlated to the length of the backlog; i.e., the larger the backlog the more likely a business will pay an expedited fee. The two-year $1 million solution adopted in 2010-11 has reduced one of the backlogs in question by nearly one-third via the expenditure of only 30 percent of the total funding appropriated. At some point, as the remaining $700,000 is expended on the two-year solution, a "tipping point" will be reached where the backlog will be low enough that businesses will no longer be paying the expedited fees at current rates of payment. This raises questions about the viability of this fund source to sustain the project's costs through its completion in 2016. Further, the "backstop" funding source, Business Fees Fund Revenues (Figure 2 above) is not much of a backstop as it has declined markedly in recent years with a 2011-12 projection of only $432,000 available for transfer (or expenditure on the Business Connect Project). This uncertainty places the GF at risk for being the true funding backstop for this project.

Second, staff notes that the current estimate of project costs is just that, an estimate, and there is not presently a level of certainty of what this project will actually cost. The FSR states the SOS conducted extensive monitoring and market research, and determined that the state with the closest system to meeting the SOS' needs was in North Carolina, yet that solution would only meet 30 to 40 percent of the SOS' needs, handles a significantly smaller volume, and has government accounting systems significantly different than California's. Therefore, the SOS reached the conclusion that a solutions-based procurement was necessary. This is a reasonable conclusion, but it translates to a level of uncertainty about costs estimates. This is not a criticism about the Business Connect Project or the materials presented by the SOS, but rather the reality of the state's process for developing this type of information technology project. Until an FSR is approved, a detailed RFP is developed, vendors bid on that RFP, which in turn drives the SPR which is submitted to the Technology Agency for its approval, a true estimate of the project's cost will not be fully known.

If the Subcommittee were to approve this request as presented it is in essence providing tacit approval for the entire Business Connect Project. Given all the factors at work, including that a true estimate of project costs is not known and there are questions about the viability of the fund source (and what impact the remaining $700,000 of the two-year solution will have on the stability of this fund source over time), providing approval of the entirety of the Business Connect Project at this juncture may be premature. Rather, in considering this request, the Subcommittee may wish to make clear it is only approving the development of the RFP, through the completion of the SPR. This would allow the Subcommittee to have at its disposal a more accurate estimate of project costs, as well as a more complete understanding of the viability of the fund source, when considering the Business Connect Project as part of a future budget cycle.

Staff Recommendation. Approve only the development of a Request for Proposal and the subsequent development of a Special Project Report for the Business Connect Project.

Vote: Staff recommendation approved by 3-0 vote.

0971 CALIFORNIA ALTERNATIVE ENERGY AND ADVANCED TRANSPORTATION AUTHORITY

Department Overview: The mission of the California Alternative Energy and Advanced Transportation Financing Authority (CAEATFA) is to promote the prompt and efficient development of energy sources which are renewable or which more efficiently utilize and conserve scarce energy resources.

January Budget Overview: The January Governor's Budget proposed total funding of $25.8 million (special funds and reimbursements) and 7.0 positions, an increase of $9.2 million and no change in positions. The year-over-year increase is primarily explained by the implementation of California Ethanol Producers Incentive Program. (See Issue 2 on the following pages for detail on this budget request).

Current Budget Status: One April Finance Letter was proposed, which is Issue #1 below.

Issue Proposed for Discussion / Vote

Issue 1 – AB 118 / California Ethanol Producers Incentive Program

Governor's Request: The Administration requests $9 million in reimbursement authority for CAEATFA to receive funds from the California Energy Commission (CEC) to perform activities related to the Alternative and Renewable Fuel and Vehicle Technology Program as authorized by AB 118 (Chapter 750, Statutes of 2007, Nunez). The specific program is the California Ethanol Producer Incentive Program (CEPIP) whereby financial assistance is provided to ethanol producers selected by CEC to develop and commercialize advanced transportation technologies that meet advanced energy goals.

Background/Detail: CAEATFA and the CEC entered into an interagency agreement that outlines the terms by which CAEATFA will assist CEC in implementing the ethanol incentive program goals. The interagency agreement is expected to have a 4-year term expiring in January 2015. The terms of the agreement allow a transfer from the CEC to CAEATFA of up to $15 million. To date, a total of $6 million has been transferred. The Governor's budget reflects a $15 million reimbursement in 2010-11 and a $9 million reimbursement in the budget year. The two-year amount requested exceeds the interagency agreement by about $9 million – CAEATFA indicates this is proposed due to uncertainty about how funds will be distributed across fiscal years, so they double-counted the $9 million.

February 10, 2011, Hearing: This issue was rejected without prejudice to allow further time for review and to consider the March 2011 AB 118 report.

Draft AB 118 Report: This year's report has been released by the CEC and states the following on the Ethanol Producers' Program:

During the administration of the CEPIP, market conditions have become increasingly unfavorable for ethanol production, particularly within California. This is due in part to near record commodity costs for corn. Given uncertain market conditions and future price projections, it is unclear whether a modest state price support program can offset the impacts of this *unprecedented change in the ethanol fuel market. As a result, the Energy Commission will reevaluate the future of the CEPIP and study the benefits from its proposed $6 million investments before making a recommendation on funding.*

Staff Comment: Given the comments in the CEC report, there are likely more cost-effective ways to expend AB 118 dollars. If the $9 million request for 2011-12 is rejected, CAEATFA and CEC can evaluate the program results for the initial $6 million and CEPIP funding could be considered again next year, if warranted.

Staff Recommendation: Deny the BCP.

Vote: On a 3-0 vote, approved a total reimbursement level of $48,000 in 2011-12, to cover the CAEATFA cost to administer the $6 million program as allocated by the California Energy Commission to the CAEATFA in 2010-11.

0840 STATE CONTROLLER'S OFFICE

Department Overview. The State Controller is the Chief Fiscal Officer of the state. The primary functions of the State Controller's Office (SCO) are to provide sound fiscal control over both receipts and disbursements of public funds; to report periodically on the financial operations and condition of both state and local government; to make certain that money due the state is collected through fair, equitable, and effective tax administration; to provide fiscal guidance to local governments; to serve as a member of numerous policy-making state boards and commissions; and, to administer the Unclaimed Property and Property Tax Postponement Programs.

Budget Overview. The January Governor's Budget provides the SCO with 1,491 authorized positions and $218.9 million ($76.5 million GF). This is an increase of two positions and $65,000.

Issues Proposed for Discussion / Vote

Issue 1 – Local Government Oversight Initiatives

April Letter Request. In an April Finance Letter, the Governor requests increased expenditure authority of $2.098 million (reimbursements) to support 16.4 existing positions to provide increased oversight of local government entities under the SCO's existing statutory authority.

Background. Generally speaking, direct state oversight of local governments is currently limited to state and federal pass-through funding. Counties receive a large share of state/federal pass-through funding to administer a number of statewide programs under state supervision, such as health and welfare. As a result, they receive direct state oversight, including SCO audits. For cities and special districts, state oversight is more limited to the few grants or allocations of state/federal pass through funding, such as Gas Tax allocations, distributed by the state. In addition, current statute provides for a more indirect oversight of local government funding using the following three elements:

1. <u>Annual Audits</u>. Each local government entity is required to have an annual audit performed by an independent auditor. If the local government has over $500,000 in federal expenditures, it must also have a single audit. Local governments are required to submit these audits to the SCO. The SCO can initiate a quality control review of the work papers of any auditor when there is suspicion that the work performed is inadequate.
2. <u>Financial Transaction Reports</u>. Statute requires the SCO to collect a report of annual financial transactions from each county, city, and special district and to publish them in reports available to the Governor, legislature, and general public. Statute further provides that, if the reports are not made in the time, form, and manner required, or if there is reason to believe a report is false, incomplete, or incorrect, the SCO shall appoint a qualified accountant to make an investigation and to obtain the information required. Statute specifies that the SCO's enforcement costs are to be reimbursed by the local government entity in question.
3. <u>Accounting and Audit Guidelines</u>. Uniform accounting guidelines are intended to provide local governments with the information necessary to implement and operate a common

accounting and reporting system. Currently such guidelines are only required for counties and special districts.

With regard to the Financial Transaction Reports, these reports represent the only source of available statewide financial data on local government entities. According to 2010 estimates, the SCO staff spent more than 1,100 hours annually on monitoring the submissions and collecting forfeitures (required payments to the state for failure to file the financial report with the SCO). The SCO indicates that the reports are subject to automated edits that do not necessarily identify all the issues that warrant attention. For instance, the SCO does not presently have the resources to compare these reports between years or between similar entities. In addition, the current analyses of all of the complaints that are being submitted to the SCO (since the City of Bell stories were reported last year) are being done through staff redirections. To the extent that an analysis results in a need for further investigation, additional redirections would be needed.

Staff Comment. The current approach is not working at an optimal level to protect taxpayers from waste, fraud, and abusive financial practices. Perhaps the greatest area where more could be done is with the financial transaction reports. This request would address that need by providing the resources to the SCO to investigate and prepare annual financial transaction reports for all non-filers, as well as conduct investigations of individual financial issues that indicate some information in an annual transaction report is "false, incorrect, or incomplete."

In considering this request, it is important to note that this request would effectively expand the use of the SCO's current statutory authorities to provide more comprehensive and coordinated oversight of local government financial practices. In theory, this would identify problems before they reach a critical stage. However, the SCO has not provided a detailed systematic plan for how it would execute the additional activities nor provided any detail regarding a benefit/cost assessment of additional financial monitoring. The audit plan submitted by the SCO is limited to a total of 47 non-filing cities and special districts for 2009-10. Based on this limited universe, the justification for funding the full request and 16.4 positions is unclear. Therefore, staff recommends this request be held open pending receipt of the requested information from the SCO.

Staff Recommendation: Hold open pending receipt of additional information.

Item held open.

Issue 2 – 21st Century Project: Related Language

April Letter Request. In an April Finance Letter, the Governor requests budget trailer bill language, as well as amended 2011-12 provisional budget bill language, to ensure deployment of the 21st Century Project.

Prior Subcommittee Action. On January 25, 2011, the Subcommittee approved \$63.7 million (\$34.2 million GF, \$1.0 reimbursements, and \$28.4 million special funds) to fund the 21st Century Project in 2011-12.

Background. The SCO pays approximately 249,000 employees, including state civil service, California State University and Judicial Council employees, judges, and elected officials. The

21st Century Project (Project) will replace the existing statewide human resource management systems in order to improve management processes and fulfill payroll and reporting obligations accurately and on time. The Project began in May 2004. The first deployment wave is scheduled for October 2011, comprised of 25 departments and 14,281 employees. That initial wave will be followed by three successive wave rollouts in January 2012 (50 departments and 75,841 employees); July 2012 (10 departments and 68,065 employees);and October 2012 (77 departments and 84,650 employees). The current estimated total cost (one-time and continuing) of the 21st Century Project is $303.2 million.

This request includes the following statutory changes related to the 21st Century project:

1. Amend Section 12432 of the Government Code to extend the SCO's existing authority to assess a variety of state funds to support the completion of the 21st Century Project. Existing law would repeal this provision on June 30, 2011. The proposed budget trailer bill language would extend the date until June 30, 2014, a date consistent with the completion of the project.
2. Amend Section 3527 of the Government Code to include a limited number of positions in the SCO's Information Systems Division (ISD), and incoming staff transfers from the 21st Century Project to the ISD, to receive and/or continue their "excluded" designation following the successful deployment of the 21st Century Project.
3. Amend Section 12420.1 of the Government Code to limit the SCO's responsibilities related to establishing employee-requested deductions for the purpose of purchasing savings bonds through the Federal Treasury Direct Program with the deployment of the 21st Century Project.

The request also includes modification of existing provisional budget bill language to allow for additional 21st Century Project funding of up to $5 million in a current fiscal year due to unforeseen circumstances and if required to ensure the successful deployment of the system. The modified language does not alter an existing requirement that the Legislature be notified in writing 30 days in advance of any adjustment being made.

Staff Comment. Budget trailer bill language is the implementing language of the California State Budget Bill. While the 21st Century Project has been, and will continue to be, funded in the annual budget act, except for the amendments to Section 12432 of the Government Code, staff has been unable to identify a direct connection between the 2011-12 budget and the other two requested amendments.

The modified provisional budget bill language is intended to address unforeseen circumstances that could arise as the 21st Century Project reaches the final stages of implementation. It provides a limit and some transparency through existing legislative notification requirements; however, there are no criteria included to indicate when such an adjustment could occur or why the SCO needs such delegated authority at this time. In addition, this modified language would set the precedent of permitting an IT project to spend up to $5 million more than its approved budget or project documents without going through some form of a budget, bill, or deficiency process. Therefore, while staff recommends adopting the modified language it would be only with a lower cap of $2 million and with supplemental report language requiring the DOF and Technology Agency, in consultation with the LAO, to develop written criteria regarding the use of this authority in the future and implement the criteria prior to the commencement of the 2012-13 budget process.

Staff Recommendation: (1) Approve the modified provisional budget bill language but with a $2 million limit and placeholder supplemental report language; (2) Approve the proposed trailer bill language amending Government Code Section 12432; and (3) Deny without prejudice the remaining proposed budget trailer bill language with direction that those changes be pursued in a policy bill.

Vote: Staff recommendation approved by 3-0 vote.

2320 DEPARTMENT OF REAL ESTATE

Department Overview. A primary objective of the Department of Real Estate (DRE) is to protect the public in real estate transactions and provide licensing, regulatory, and subdivision services to the real estate industries. The DRE is entirely special funded (Real Estate Fund) and derives its revenues from examination, license, and subdivision fees. The core functions of the DRE are to administer license examinations, issue real estate licenses, regulate real estate licensees, and qualify subdivision offerings.

Budget Overview. The January Governor's Budget provides DRE with 381 authorized positions and $46.0 million (RE Fund and reimbursements). This is an increase of two positions and $1.5 million.

Issue Proposed for Discussion / Vote

Issue 1 – Sacramento Headquarters and Examination Center Consolidation and Relocation

April Letter Request. In an April Finance Letter, the Governor requests increased expenditure authority of $2.612 million (Real Estate Fund) to relocate and consolidate into one location on or about January 1, 2012, the DRE's Sacramento Headquarters Office and Examination Center. Figure 3 below summarizes the components of this request:

Figure 3

	2011-12	2012-13	2013-14
Six months rent increase January 1 through June 30, 2012	$635,500*		
Moving related expenses	$1,220,000*		
Tenant Improvements	$756,000*		
Increased rent costs for twelve months (July 1, 2012, through June 30, 2013)		$1,271,000	
Six months of scheduled lease cost increase ($.07 per square foot of office space)		$31,500	
Ongoing lease cost increases over term of lease			$63,000
TOTAL	$2,611,500*	$1,302,500	$63,000**

*2011-12 costs are all one-time.
**Increased amount continues through Fiscal Year 2019-20.

Prior Subcommittee Action. As part of the 2009-10 budget, the Governor requested a one-time augmentation of $1 million (Real Estate Fund) to partially cover the estimated costs ($1.3-$1.5 million) to relocate and consolidate the DRE's downtown Sacramento Headquarters Office and Examination Center at a new location. At that time, staff did not necessarily dispute DRE's claim that the existing facilities did not meet the long-term needs of the department and once increased rent and the cost of a double move were factored in. However, the Subcommittee rejected the request due to the fact that the Real Estate Fund had a structural deficit.

As part of the 2010-11 budget, the DRE did not present a request related to its Headquarters relocation and consolidation; rather, the DRE proposed to absorb those costs from within its existing budget. The Subcommittee did not agree with this approach, due to concerns that doing so could result in decreased enforcement and consumer protection activities. The Subcommittee instead requested that the DRE present a formal request related to its facility needs during the 2011-12 budget process.

Background. The DRE's Headquarters and Examination Center facilities have been located in their present locations in downtown Sacramento since 1985. The DRE leases a total of 44,922 square feet at a cost of $1.75 per square feet. The current lease expires on September 30, 2011, and will thereafter convert to a month-to-month soft-term lease agreement. The amount of leased space has not changed during the 26 years the DRE has been at this location; therefore, the current facilities present significant space constraints. Since 1985, the DRE's licensee population and the associated workload and file storage requirements have increased by 70 percent; there were 268,842 licensees in 1985, and a total of 457,113 today. In addition, the DRE was recently required to add a new licensing and enforcement program for mortgage loan originators. The DRE has also absorbed a 38 percent increase in staff levels, from 144 staff in January 1987 (accurate earlier data unavailable) to a total of 198 today. In addition, the current facilities present significant health and safety concerns and deterioration problems. The DRE also cannot offer electronic license examinations in the current exam center without extensive renovations and costs; current estimates are that the costs could approach $900,000 based on renovations of similar exam facilities.

Working with the DGS' Real Estate Leasing and Planning Section, the DRE is considering several new locations within the City of Sacramento, as required by current law. The request before the Subcommittee represents a new facility comprised of a total of 75,000 square feet of office space at an estimated cost of $2.40 per square foot and 10,000 square feet of warehouse space at an estimated cost of $.45 per square foot, for a total estimated lease cost of $2.214 million per year. The DRE is presently paying $943,000 per year for its current facilities; the new location would therefore represent a net increase of $1.271 million per year in lease costs. The DGS is proposing a lease term of eight years, with the first four years termed "firm," and the second four years termed "soft." According to DGS, the eight year lease is a state product and has been in use for about ten years.

The one-time moving costs are estimated to total $1.22 million, including: (1) $990,000 for Modular Systems Furniture; (2) $115,000 in moving expenses; (3) $46,000 to install telecommunications systems; (4) $46,000 for network switches, cabling, and electrical costs; and (5) $23,000 for supplies such as business cards, stationary, etc.

Staff Comment. Staff concurs with the need to relocate and consolidate the DRE's Sacramento Headquarters and Examination Center facilities into a single location, thereby achieving a more efficient operation and a safer working environment, for both employees, licensees, and the general public. Remaining in the current location is not an option, neither is renovating the current facility as that option would require costly improvements and do nothing to address the fact that the DRE has simply outgrown its current space. This latter option would also involve double moving costs.

Staff notes that this request is built upon estimated lease costs of $2.40 per square foot for office space and $.45 per square foot of warehouse space. The DGS has indicated, however, that given current conditions in the commercial real estate market it is likely that DRE's office lease costs will result in a final cost of $2.00 per square foot, with a similar level of reduction in warehouse lease costs. Therefore, in considering this request, the Subcommittee may wish to adopt provisional budget bill language to ensure that any unused funds appropriated in 2011-12 for lease terms are not built into the DRE's base budget.

Staff Recommendation: Approve the request and adopt placeholder provisional budget bill language to state that the DRE cannot redirect amounts in excess of agreed-upon relocation and consolidation costs, including lease terms, to other purposes.

Vote: Staff recommendation approved by 3-0 vote.

8955 CALIFORNIA DEPARTMENT OF VETERANS AFFAIRS

Department Overview. The California Department of Veterans Affairs (CDVA) promotes and delivers benefits to California veterans and their families. More specifically, the CDVA provides: (1) California veterans and their families with aid and assistance in presenting their claims for veterans' benefits under the laws of the United States; (2) California veterans with beneficial opportunities through direct low-cost loans to acquire farms and homes; and (3) the state's aged and disabled veterans with rehabilitative, residential, and medical care and services in a home-like environment at the Veterans Homes of California (VHCs). The CDVA operates VHCs in Yountville (Napa County), Barstow (San Bernardino County), Chula Vista (San Diego County), and Greater Los Angeles Ventura County (with homes in West Los Angeles, Ventura, and Lancaster).

Budget Overview. The January Governor's Budget proposes to continue to ramp-up admissions at the VHCs in West Los Angeles, Lancaster, and Ventura. The Governor also proposes to provide continued resources and staffing related to the construction and activation of two new VHCs, in Redding and Fresno, both of which are scheduled to begin admissions in early calendar year 2012. The January Governor's Budget provides CDVA with 2,396.5 authorized positions and $399.3 million ($253.4 million GF).

Issue Proposed for Discussion / Vote

Issue 1 – Central Coast Veterans Cemetery Project: Preliminary Plans

April Letter Request. In an April Finance Letter, the Governor requests that two new items be added to the 2011-12 budget to transfer and then appropriate $1.074 million for the preliminary plans phase of the Central Coast Veterans Cemetery project.

Background. Military and Veterans Code Section 1450 et seq. required the CDVA to develop a master plan for a Central Coast Veterans Cemetery Project, a state-owned and operated veterans' cemetery on the grounds of the former Fort Ord in Monterey County. To fund the Cemetery Project, the original 2000 statute provided $140,000 GF seed money for the master plan and created two funds: (1) the California Central Coast State Veterans Cemetery at Fort Ord Endowment Fund (Endowment Fund); and (2) the California Central Coast State Veterans Cemetery at Fort Ord Operations Fund (Operations Fund). The Endowment fund is the mechanism for local entities to provide funding for the development and operation of the Cemetery Project. The Operations Fund receives its funding via transfer from the Endowment Fund to support the costs of designing, constructing, and maintaining the Cemetery Project. To protect the state, and before a transfer can be made, statute requires a Director of Finance determination that adequate funds exist in the Endowment Fund to fully complete the preliminary plans (as well as working drawings).

Per the master plan, the Cemetery Project would utilize a portion of a 79-acre site and accommodate the remains of nearly 14,000 veterans and spouses. It is expected that the Cemetery Project would accommodate anticipated burials for the next 20 years and that the full 79-acre site, once eventually developed, is adequate to meet burial demand for the next 100 years. The total Cemetery Project costs of $27.0 million would be funded through a mixture of local moneys transferred into the Endowment Fund and federal funds, with the federal funds providing all of the construction costs and reimbursement of most of the design costs.

The April letter before the Subcommittee would add item 8955-011-0848 to the 2011-12 budget to transfer $1.074 million from the Endowment Fund to the Operations Fund. In addition, the April letter requests that item 8955-301-3013 be added to the 2011-12 budget to appropriate $1.074 million from the Operations Fund for the preliminary plans phase of the Cemetery Project.

Statute also requires the State Controller's Office to annually report the amount of interest and investment earnings generated by the Endowment Fund and the estimated amount of additional principal needed to generate annual interest revenue that will sufficiently fund the estimated annual administrative and oversight costs. The most recent report, dated July 22, 2010, reported that no deposits were made to the Endowment Fund and the fund remained with a zero cash balance for the fiscal year ended June 30, 2010, and prior. Therefore, no interest or investment earnings were generated.

Staff Comment. This April letter requests to add items to the budget to transfer nonexistent funds from an Endowment Fund to an Operations Fund and then appropriate those nonexistent funds to cover the costs of preliminary plans for the Central Coast Veterans Cemetery Project. When queried on this approach, the Administration indicated that while it is not commonly utilized its purpose is to show good faith on the part of the state with the local entities that support and are raising funds for the Cemetery Project. The local entities presently fear that if they deposit funds raised (currently $160,000) into the Endowment Fund they have no assurance that the state will then in turn appropriate the funds for preliminary plans, which is the first phase or step to realizing the Cemetery Project. Given the state's fiscal condition, this fear is understandable, and has also potentially impacted the local entities' ability to raise funds. Were this request to be approved, local entities could therefore have an enhanced ability to raise funds as they have "proof" of the state's intent to support the Cemetery Project.

According to the Administration, this approach was used in the 2001-01 budget to authorize a predominantly privately funded project to renovate and expand the Lincoln Theater at the Veterans Home of California Yountville prior to the private funds being in place. More recently, the 2010-11 budget includes three Department of Parks and Recreation projects that are to be funded by private non-profits. In this case, the funds were not set-aside at the time of appropriation, which is why Provision 2 was added to state, "*The funds in this item shall not be expended without prior approval from the Department of Finance*."

As noted in the background section above, current statute contains checks and balances to prevent moving forward on the preliminary plans without the total required funding being deposited into the Endowment Fund. Further, current statute delineates a process whereby the subsequent phases of the Cemetery Project (i.e., working drawings and construction) will proceed only when funds are available as determined by the Director of Finance. This April letter is limited to the first phase – preliminary plans. Therefore, in considering this request, the Subcommittee may wish to modify the Administration's budget bill language to include a citation to the relevant statute.

Staff Recommendation: Approve the April letter with modified budget bill language citing the relevant Military and Veterans Code statute.

Vote: Staff recommendation approved by 3-0 vote.

SUBCOMMITTEE NO. 4 Agenda

Senator Michael J. Rubio, Chair
Senator Doug La Malfa
Senator Noreen Evans

Thursday, May 26, 2011
10:00 a.m.
Room 112

Consultant: Keely Martin Bosler and Brian Annis

AGENDA PART A

Item	Department	Page

Pursuant to the Americans with Disabilities Act, individuals who, because of a disability, need special assistance to attend or participate in a Senate Committee hearing, or in connection with other Senate services, may request assistance at the Senate Rules Committee, 1020 N Street, Suite 255 or by calling 916-324-9335. Requests should be made one week in advance whenever possible.

AGENDA – VOTE ONLY ITEMS

AGENDA – DISCUSSION / VOTE ITEMS

Vote Only Calendar

1730 Franchise Tax Board

1. Enterprise Data to Revenue Project

Background. The Franchise Tax Board's (FTB's) tax filing system has not been substantially updated in the last 25 years. In order to modernize the FTB's filing system, the board initiated the Enterprise Data to Revenue (EDR) Project two years ago. This project will introduce a new Personal Income Tax (PIT) and Business Entity return processing system including expanded imaging, data capture, and return validation. Annually, the FTB processes approximately 15 million PIT returns and one million Business Entity returns. Overall, this project will enable FTB to correct erroneous returns in a timelier manner. It will also be more effective at providing data to identify noncompliance patterns and help identify fraudulent activity. This data system will also allow FTB to better prioritize its workload based on highest cost recovery. The FTB indicates that the new system will also expand self-help tools for taxpayers and tax practitioners to improve the filing and payment activities.

The FTB is using an alternate type of procurement for the EDR project that invites bidders to propose a comprehensive solution to address the overall goals outlined by the EDR project, instead of dictating the solution to the bidders. In this type of procurement, the State enters into a contract with a Primary Solution Provider (PSP) and the State works collaboratively with the provider to find a solution that meets the goals of the State. The FTB received proposals last year and chose a PSP in November 2010.

The FTB is also using a benefits based procurement model to acquire the EDR Project and get the best value and business driven solution. This model is based on acquiring innovative 23 solutions to strategic business problems and only compensating the contractor when these solutions deliver new tax revenues and after certain State costs are recouped. Revenue benefits are then shared with the contractor up to a fixed contract amount. Furthermore, the contract is constructed so that the State does not incur upfront expenses to compensate the contractor.

When fully implemented, the FTB estimates that the EDR project will bring in over $1 billion in ongoing revenue annually. This will help to address the $6.5 billion annual tax gap through increased collection of tax revenues that are due to the State but currently unpaid or uncollected for various reasons. Overall, the one-time costs of the PSP contract are estimated to be $398.9 million over the life of the 66-month (5.5 year) contract. This is significantly more than earlier anticipated costs of the project ($234 million). However, the State is now estimating that the proposed solution by the vendor will generate approximately $1 billion more in revenues over the life of the project.

Finance Letter. The Governor's April 1 Finance Letter requests $28.9 million General Fund to support the EDR project in the budget year. Last year, the Legislature approved a $10.2 million request, including 72 new positions. These costs will be more than offset by the additional revenues that the FTB estimates will be received in the 2011-12 fiscal year. The FTB anticipates generating $65.3 million in additional revenues in 2011-12 which is nearly $40 million more than initially anticipated prior to the FTB receiving the PSP solution.

Specifically, the funding requested in the budget year supports the following expenditures:

1. Personal Services. Includes $3.9 million for support of personal services. However, no additional positions are provided in this budget proposal. The department has indicated that it will redirect existing vacant positions to support this proposal in the short term.
2. PSP Contract. Initial compensation benefits ($25 million) to the PSP paid from additional revenues collected due to the implementation of several "early win" deliverables that will result in additional revenues in the first two to 18 months. Some of the early win deliverables are business process changes that do not require the entire information technology solution to be in place, including making changes to the tax forms to adjust for common mistakes related to real estate deductions and adding additional fields of data to the Accounts Receivable Collection System database.
3. Independent Verification and Validation (IV&V) Contract. Funding ($1.3 million) to acquire an IV&V contractor which is a standard practice of the State when entering into contracts for large information technology projects.
4. Cost Reasonableness Contract. Funding ($110,000) for Cost Reasonableness consultant services. This consultant will act as another check and balance on the main PSP contract to ensure that the costs charged to the State in delivering the project are reasonable and not outside the normal industry standards.

Staff Comments. Overall, staff finds that the EDR project has been thoroughly planned and the FTB has obviously done significant work to ready the organization for the implementation of the new system, including a complete documentation of their business processes. However, the proposed solution by the PSP has a considerably different cost and revenue structure than originally estimated. It will be critical that the state monitor how the estimated cost and revenue structure of this project tracks with actual revenues and expenditures. Furthermore, the calculation of the revenues attributable to the EDR project is essential to evaluating the relative value of the PSP contract. This issue was heard and left open at the May 5 Subcommittee #4 hearing pending receipt of the 2010-11 Section 11 request. The Section 11 request is notification to the Joint Legislative Budget Committee that the Department intends to sign the vendor contract – that Section 11 request was received on May 13.

Staff Recommendation. Staff recommends that the Subcommittee approve this budget request.

8860 Department of Finance

1. Office of the Inspector General - Reorganization

Background. The Office of State Audits and Evaluations (OSAE) is an office within the Department of Finance (DOF) that supports DOF in supervising the state's financial and business policies and in conserving the state's rights, interests, and resources. OSAE accomplishes this through independent audits, objective evaluations, and other related services.

May Revision. The May Revision proposes reorganizing and streamlining the responsibilities of the Office of the Inspector General (OIG). As part of this reorganization, the Administration proposes to transfer workload related to inspections of health care services at the state prisons from the OIG to OSAE. The OSAE would be responsible for evaluations of health care in the prisons and would provide reports to the federal court.

Staff Comments. Staff finds that at this time transferring the workload associated with the prison health care audits seems to create some unknown risk in respect to ultimately satisfying the demands of the *Plata* court while achieving minimal savings.

Staff Recommendation. Staff recommends rejecting this proposal, which is conforming to an action being taken by Subcommittee 5 on the overall reorganization of the OIG.

Revenues

1. Maintain Existing Taxes: Realignment

Governor's Budget and 2011 Budget Conference Committee. The Governor's budget proposed a constitutional amendment to maintain the current sales tax and VLF rates for a five year period dedicated to local governments to support **$5.9 billion** in public safety programs that would be realigned from the state to the counties. The 2011 Budget Conference Committee approved this measure in March of this year, as follows:

- **Maintain 1 percent Increase to State Sales and Use Tax.** The State Sales and Use Tax rate was increased from 5 percent to 6 percent effective April 1, 2009. The increase is set to sunset on June 30, 2011. The Governor's budget would extend the 1 percent State Sales and Use Tax for five additional years to support local public safety programs. This proposal is expected to generate $4.5 billion in the budget year.
- **Maintain 0.5 percent Increase to VLF.** The rate of the vehicle license fee (VLF) was increased from 0.65 to 1.15 percent of a vehicle's value, effective May 19, 2009 and will sunset on June 30, 2011. The increase from 0.65 to 1 percent went to benefit the General Fund and 0.15 of the increase was transferred to the Local Safety and Protection Account to fund local law enforcement programs. The Governor's budget would maintain this increase for five additional years to support local public safety programs, including the local public safety programs supported by the 0.15 raised in 2009. This proposal is expected to generate $1.4 billion in the budget year.

May Revision. The Governor has modified the realignment proposal to reduce the public safety programs being realigned by approximately $270 million. The Governor is therefore reducing the revenues dedicated to realignment commensurately. Instead of dedicating all 0.5 percent of the VLF, the Governor now proposes to dedicate 0.4 percent of the VLF to realignment and the remaining 0.1 percent to the General Fund to support schools. The Governor does not propose any changes to the Sales Tax extension.

Staff Recommendation. Staff recommends that the Subcommittee approve the May Revision proposal to modify the allocation of the VLF to reflect the revised realignment proposal.

2. Maintain Existing Taxes: Education

Governor's Budget and 2011 Budget Conference Committee. The Governor's budget proposed a constitutional amendment maintaining the following tax rates for a five year period dedicated to education that will generate **$5.2 billion** annually. The 2011 Budget Conference Committee approved this measure in March of this year, as follows:

- **Maintain 0.25 percent Surcharge.** A PIT surcharge of 0.25 percent was enacted effective in the 2009 and 2010 tax years. The Governor's budget estimates that maintaining this surcharge would generate $3.3 billion in the current and budget years.
- **Maintain Reduced Dependent Exemption Credit.** The dependent exemption credit was reduced from $309 to $99 effective in the 2009 and 2010 tax years. The Governor's budget estimates that maintaining this reduced credit will generate about $2 billion in the current and budget years.

May Revision. The Governor has proposed to reduce the tax package proposed in January by eliminating the 0.25 percent surcharge for the 2011 tax year. The Governor does propose to reinstate the 2010 tax rate in the 2012 tax year for a four year period. This change reduces the tax package by $2 billion relative to the Governor's budget. The Governor does not propose any changes to the dependent credit proposal.

Staff Recommendation. Staff recommends that the Subcommittee approve the Governor's elimination of the 0.25 percent surcharge for the 2011 tax year.

3. Targeted Tax Expenditures: Enterprise Zones

Background. Existing law provides special tax incentives for four kinds of geographically targeted economic development areas. These areas include enterprise zones, local agency military base recovery areas (LAMBRAs), manufacturing enhancement areas (MEAs), and targeted tax areas (TTAs). The tax incentives enjoyed by businesses located in these areas include accelerated depreciation, 100 percent net operating loss carryover, wage credits, and credits for sales tax on equipment purchased for use in the zone. There are some differences among the tax incentives provided for each area, but taxpayers generally have access to each form of preferable tax treatment.

The law currently limits the number of enterprise zones (42), LAMBRAs (8), MEAs (2) and TTAs (1). The Department of Housing and Community Development has designated 42 enterprise zones and 7 LAMBRAs as of December 15, 2010.

Employers within enterprise zones are allowed to claim a tax credit of 50 percent of the wages paid to a qualified employee in the first year, 40 percent in the second year, 30 percent in the third year, 20 percent in the fourth year, and 10 percent in the fifth year, up to 150 percent of the minimum wage. Qualified employees include individuals: (1) eligible for job training programs; (1) eligible for most social welfare programs; (3) economically disadvantaged; (4) dislocated workers; (5) disabled and eligible or enrolled in a state rehabilitation plan; (6) veteran; (7) ex-offender; and (8) member of a federally recognized Indian Tribe. Furthermore, existing law also allows enterprise zones to designate targeted employment areas (TEAs) to contain census tracts where 51 percent or more of individuals are considered low or moderate income. Any hire made out of a TEA can qualify the taxpayer in the enterprise zone for the hiring tax credit and TEAs can be drawn outside the borders of the enterprise zones.

The tax expenditures related to these zones cost the state approximately **$300 million** annually.

Governor's Budget and 2011 Budget Conference Committee. The Governor's budget proposed to repeal the state tax benefits allowed in the four kinds of geographically targeted economic development areas described above. The proposal would have eliminated all state tax benefits for both newly earned credits and deductions and for credits that had been earned in prior years, but have not been used. Local agencies would have the option of keeping their local incentives. This proposal would have generated additional revenues of **$924 million** in the current and budget years. The 2011 Budget Conference Committee also approved this proposal.

May Revision. The Governor's May Revision withdraws the January proposal to repeal the tax benefits for enterprise zones. Instead the Governor proposes to reform enterprise zone hiring credits so that credits are only available to firms which actually increase their level of employment. Under the new hiring credit the taxpayer would be eligible for a $5,000 credit for each incremental full-time equivalent employee that they hire. These credits would be allowed if claimed on the taxpayer's original return.

Furthermore, the May Revision proposal limits a practice known as "retro-vouchering" by not allowing any new vouchers to be granted for tax years prior to 2011 when the application for that voucher was made more than 30 days after the date that the employee first begins employment. The May Revision proposes to limit enterprise zone credits to a five year carry-forward period to ensure that the credit is encouraging relatively profitable businesses.

This proposal would generate additional revenues of **$93 million** in the current and budget years.

Good Goal, But Not a Core State Responsibility. The enterprise zone program was formed in 1984 to help draw investment into depressed rural and urban areas. While this is a good goal, it is not a core responsibility of state government and given the state's chronic budget deficits it is important that all state spending, including tax expenditures be scrutinized. Furthermore, the Governor has proposed a new option for local governments that want to continue to fund economic development activities. Specifically, the Governor has proposed a constitutional amendment to provide for 55 percent voter approval for limited tax increases and bonding against local revenues for economic development projects.

Current Program Not Proven Effective. In addition, the LAO and others have found that enterprise zone tax benefits have little to any impact on the creation of economic activity or employment in California. The LAO found that the program mainly seemed to shift economic activity from one zone to another within California without doing anything to grow economic activity. Furthermore, there is some evidence that benefits from the enterprise zone program go to taxpayers whose behavior has not been affected at all by the program, but instead by firms that specialize in finding businesses that could benefit from the program and offering to prepare the taxpayers tax return on a percent of benefit basis. In these cases it is clear that the taxpayer did not relocate their business because of the enterprise zone – since they had to be told of the tax benefit after they had already relocated.

Reform versus Elimination. Recently there have been significant efforts to make some reforms to the enterprise zone program. Specifically, SB 974 (Steinberg) from 2010 proposed to eliminate Targeted Employment Areas (TEAs) and stop the practice of retro-vouchering. As mentioned above, TEAs allow a taxpayer to qualify an employer for a tax credit not based on who they are, but based solely on residence within a zip code range listed on his or her employment records. Retro vouchering essentially allows taxpayers to gain tax credits for hiring decisions made in the past. Taxpayers often use the TEA criterion and the retro-vouchering to check payroll records and essentially "mine" the data for qualified employees and then file tax claims for refunds with the State.

Staff Comment: With the May Revision, the Governor is proposing to maintain, but reform, the enterprise zone program. The reformed program would become more focused on job creation, which is one of the highest priorities of the state at this time.

Staff Recommendation. Staff recommends that the Subcommittee take the following actions:

- Withdraw the proposal to eliminate all tax incentives in enterprise zones.
- Approve trailer bill language to reform enterprise zone hiring credits.

4. Jobs Tax Credit Expansion

Background. As part of the February 2009 budget package, the Legislature adopted SB X3 15 (Calderon) that included provisions to incentivize small business job creation through a small-business hiring tax credit. The legislation allows a qualified employer to claim an income tax credit of $3,000 for each additional full-time employee hired by the employer during the taxable years 2009 and 2010. Unused credits may be carried forward by the taxpayer to reduce the tax liability over the following eight years. The total taxpayer benefits – and General Fund revenue loss – from the credits is capped at $400 million. The amount of credit is prorated if the employee works fewer than 12 months during the employer's tax year. The credit is only available to a business that has 20 or fewer employees on the first day of the taxable year. When SB X3 15 was adopted, the revenue estimates assumed most of the credits would be both claimed and used to offset tax liability in the short term – reducing State tax revenue in 2008-09 and 2009-10 by a total of $345 million. However, the Administration indicates only about $36 million in credits were used to offset revenue in 2008-09 and 2009-10.

May Revision. The Governor's May Revision proposes to expand the job credit to further stimulate small business job creation. The credit would be extended into the 2011 and 2012 tax years, the credit would be increased from $3,000 to $4,000 per new job created, and the credit would be available to more employers by expanding the definition of small business from 20 or fewer employees, to 50 or fewer employees. Other components of the tax credit would remain unchanged such as the cap of $400 million for the program. Since the credit was not fully allocated in the 2009 and 2010 tax years and would now be extended to 2011 and 2012 tax years, this proposal does result in addition General Fund revenue loss relative to the baseline forecast. The revenue loss in 2010-11 is estimated by the Department of Finance at $29 million and the revenue loss in 2011-12 is estimated at $65 million.

Related May Finance Letter for the BT&H Agency. The Governor is also proposing to augment the budget of the Business, Transportation and Housing Agency (BT&H Agency) by $279,000 General Fund to add one position and fund consulting services, to increase public awareness of the tax credit. The Administration did not provide the typical Finance Letter detail with this proposal that would explain the activities of the new state staff and the consultant.

Staff Comment: While not explicitly linked to other revenue proposals in proposed trailer bill language, this proposal is a new tax expenditure that would reduce General Fund revenues by an estimated $94 million through June 2012. This new tax expenditure program would be difficult to fund in this constrained budget environment unless the Governor's tax extensions and tax policy reforms are also adopted. New General Fund expenditures of $279,000 are proposed marketing the program, but public outreach could also be accomplished within existing state resources such as press officers and Agency Secretaries that could publicize the program with speeches to local chambers of commerce, press events, etc.

Staff Recommendation. Staff recommends that the Subcommittee take the following actions:

- Approve trailer bill language to expand the jobs credit.
- Reject the $279,000 General Fund at the BT&H Agency for marketing the program, and instead achieve improvements to public outreach with existing resources.

5. Sales and Use Tax Exemption—Manufacturing Equipment

Background. For a ten-year period ending December 31, 2003, California law provided a partial (General Fund only) sales and use tax exemption for purchases of equipment and machinery by new manufacturers, and income and corporation tax credits for existing manufacturers' investments (MIC) in equipment. The sales and use tax exemption provided relief of payment of the state tax portion for purchases of qualifying property, and the income tax credit was equal to six percent of the amount paid for qualified property placed in service in California. New manufacturers could either receive the benefit of the exemption, or claim the income tax credit. However, existing manufacturers could only receive the benefit of the income tax credit. This sales and use tax exemption and income tax credit had a conditional sunset date that was triggered when manufacturing employment (as determined by the Employment Development Department) did not exceed manufacturing employment as of January 1, 1994 by more than 100,000 workers. On January 1, 2003, manufacturing employment was less than the 1994 number by over 10,000 workers, and therefore the MIC and partial sales tax exemption expired at the end of 2003.

May Revision. The Governor's May Revision proposes to provide a new partial sales and use tax exemption for qualified purchases by a taxpayer involved in manufacturing starting July 1, 2012 and ending July 1, 2016. This exemption is similar to the exemption in state law from 1994 until 2003, but has differential exemptions for existing and new manufacturers. It is intended to decrease the cost of doing business for manufacturing companies in an attempt to stimulate investment and employment in those industries and to attract and expand business activity in California. The proposed credit would provide a full 5-percent exemption of the General Fund sales and use tax for new start-up firms and a 1-percent exemption for existing firms. The State General Fund revenue loss from the proposal is estimated at $261 million in 2012-13, increasing slightly thereafter through 2015-16.

Linked to Other Revenues. The proposed sunset for the manufacturers' tax exemption of July 1, 2016, is linked to the date the temporary taxes would expire. The proposed trailer bill language would make the new tax expenditure contingent on voter approval of a proposition on a future statewide general election ballot related to the tax extensions. These tax extensions are the sales tax and Vehicle License Fee revenues dedicated to realignment (see also agenda issue #1) and the personal income tax revenues dedicated to education (see also agenda issue #2). While not explicitly linked in the proposed trailer bill language, the Governor's May Revision document indicates the manufacturers' credit is not affordable unless his proposal is adopted to make the single sales factor mandatory. Note, the single sales factor proposal was adopted by the Budget Conference Committee, and the Governor proposed no change in the May Revision.

Staff Comment: As indicated above, this proposal is a new tax expenditure that would reduce General Fund revenues by an estimated $261 million in 2012-13. This new tax expenditure program would be difficult to fund in this constrained budget environment unless the Governor's tax extensions and tax policy reforms are also adopted.

Staff Recommendation. Approve trailer bill language to create a new manufacturers' tax credit contingent on the maintenance of existing taxes.

Senate Budget and Fiscal Review—Mark Leno, Chair

SUBCOMMITTEE NO. 4 Agenda

Senator Michael J. Rubio, Chair
Senator Doug La Malfa
Senator Noreen Evans

Hearing Outcomes

Thursday, May 26, 2011
10:00 a.m.
Room 112

Consultant: Keely Martin Bosler and Brian Annis

AGENDA PART A

State Administration and General Government

Pursuant to the Americans with Disabilities Act, individuals who, because of a disability, need special assistance to attend or participate in a Senate Committee hearing, or in connection with other Senate services, may request assistance at the Senate Rules Committee, 1020 N Street, Suite 255 or by calling 916-324-9335. Requests should be made one week in advance whenever possible.

AGENDA – VOTE ONLY ITEMS

AGENDA – DISCUSSION / VOTE ITEMS

Vote Only Calendar

1730 Franchise Tax Board

1. Enterprise Data to Revenue Project

Background. The Franchise Tax Board's (FTB's) tax filing system has not been substantially updated in the last 25 years. In order to modernize the FTB's filing system, the board initiated the Enterprise Data to Revenue (EDR) Project two years ago. This project will introduce a new Personal Income Tax (PIT) and Business Entity return processing system including expanded imaging, data capture, and return validation. Annually, the FTB processes approximately 15 million PIT returns and one million Business Entity returns. Overall, this project will enable FTB to correct erroneous returns in a timelier manner. It will also be more effective at providing data to identify noncompliance patterns and help identify fraudulent activity. This data system will also allow FTB to better prioritize its workload based on highest cost recovery. The FTB indicates that the new system will also expand self-help tools for taxpayers and tax practitioners to improve the filing and payment activities.

The FTB is using an alternate type of procurement for the EDR project that invites bidders to propose a comprehensive solution to address the overall goals outlined by the EDR project, instead of dictating the solution to the bidders. In this type of procurement, the State enters into a contract with a Primary Solution Provider (PSP) and the State works collaboratively with the provider to find a solution that meets the goals of the State. The FTB received proposals last year and chose a PSP in November 2010.

The FTB is also using a benefits based procurement model to acquire the EDR Project and get the best value and business driven solution. This model is based on acquiring innovative 23 solutions to strategic business problems and only compensating the contractor when these solutions deliver new tax revenues and after certain State costs are recouped. Revenue benefits are then shared with the contractor up to a fixed contract amount. Furthermore, the contract is constructed so that the State does not incur upfront expenses to compensate the contractor.

When fully implemented, the FTB estimates that the EDR project will bring in over $1 billion in ongoing revenue annually. This will help to address the $6.5 billion annual tax gap through increased collection of tax revenues that are due to the State but currently unpaid or uncollected for various reasons. Overall, the one-time costs of the PSP contract are estimated to be $398.9 million over the life of the 66-month (5.5 year) contract. This is significantly more than earlier anticipated costs of the project ($234 million). However, the State is now estimating that the proposed solution by the vendor will generate approximately $1 billion more in revenues over the life of the project.

Finance Letter. The Governor's April 1 Finance Letter requests $28.9 million General Fund to support the EDR project in the budget year. Last year, the Legislature approved a $10.2 million request, including 72 new positions. These costs will be more than offset by the additional revenues that the FTB estimates will be received in the 2011-12 fiscal year. The FTB anticipates generating $65.3 million in additional revenues in 2011-12 which is nearly $40 million more than initially anticipated prior to the FTB receiving the PSP solution.

Specifically, the funding requested in the budget year supports the following expenditures:

1. Personal Services. Includes $3.9 million for support of personal services. However, no additional positions are provided in this budget proposal. The department has indicated that it will redirect existing vacant positions to support this proposal in the short term.
2. PSP Contract. Initial compensation benefits ($25 million) to the PSP paid from additional revenues collected due to the implementation of several "early win" deliverables that will result in additional revenues in the first two to 18 months. Some of the early win deliverables are business process changes that do not require the entire information technology solution to be in place, including making changes to the tax forms to adjust for common mistakes related to real estate deductions and adding additional fields of data to the Accounts Receivable Collection System database.
3. Independent Verification and Validation (IV&V) Contract. Funding ($1.3 million) to acquire an IV&V contractor which is a standard practice of the State when entering into contracts for large information technology projects.
4. Cost Reasonableness Contract. Funding ($110,000) for Cost Reasonableness consultant services. This consultant will act as another check and balance on the main PSP contract to ensure that the costs charged to the State in delivering the project are reasonable and not outside the normal industry standards.

Staff Comments. Overall, staff finds that the EDR project has been thoroughly planned and the FTB has obviously done significant work to ready the organization for the implementation of the new system, including a complete documentation of their business processes. However, the proposed solution by the PSP has a considerably different cost and revenue structure than originally estimated. It will be critical that the state monitor how the estimated cost and revenue structure of this project tracks with actual revenues and expenditures. Furthermore, the calculation of the revenues attributable to the EDR project is essential to evaluating the relative value of the PSP contract. This issue was heard and left open at the May 5 Subcommittee #4 hearing pending receipt of the 2010-11 Section 11 request. The Section 11 request is notification to the Joint Legislative Budget Committee that the Department intends to sign the vendor contract – that Section 11 request was received on May 13.

Staff Recommendation. Staff recommends that the Subcommittee approve this budget request.

Action: Approved staff recommendation on a 3 – 0 vote.

8860 Department of Finance

1. Office of the Inspector General - Reorganization

Background. The Office of State Audits and Evaluations (OSAE) is an office within the Department of Finance (DOF) that supports DOF in supervising the state's financial and business policies and in conserving the state's rights, interests, and resources. OSAE accomplishes this through independent audits, objective evaluations, and other related services.

May Revision. The May Revision proposes reorganizing and streamlining the responsibilities of the Office of the Inspector General (OIG). As part of this reorganization, the Administration proposes to transfer workload related to inspections of health care services at the state prisons from the OIG to OSAE. The OSAE would be responsible for evaluations of health care in the prisons and would provide reports to the federal court.

Staff Comments. Staff finds that at this time transferring the workload associated with the prison health care audits seems to create some unknown risk in respect to ultimately satisfying the demands of the *Plata* court while achieving minimal savings.

Staff Recommendation. Staff recommends rejecting this proposal, which is conforming to an action being taken by Subcommittee 5 on the overall reorganization of the OIG.

Action: Approved staff recommendation on a 3 – 0 vote.

Revenues

1. Maintain Existing Taxes: Realignment

Governor's Budget and 2011 Budget Conference Committee. The Governor's budget proposed a constitutional amendment to maintain the current sales tax and VLF rates for a five year period dedicated to local governments to support **$5.9 billion** in public safety programs that would be realigned from the state to the counties. The 2011 Budget Conference Committee approved this measure in March of this year, as follows:

- **Maintain 1 percent Increase to State Sales and Use Tax.** The State Sales and Use Tax rate was increased from 5 percent to 6 percent effective April 1, 2009. The increase is set to sunset on June 30, 2011. The Governor's budget would extend the 1 percent State Sales and Use Tax for five additional years to support local public safety programs. This proposal is expected to generate $4.5 billion in the budget year.
- **Maintain 0.5 percent Increase to VLF.** The rate of the vehicle license fee (VLF) was increased from 0.65 to 1.15 percent of a vehicle's value, effective May 19, 2009 and will sunset on June 30, 2011. The increase from 0.65 to 1 percent went to benefit the General Fund and 0.15 of the increase was transferred to the Local Safety and Protection Account to fund local law enforcement programs. The Governor's budget would maintain this increase for five additional years to support local public safety programs, including the local public safety programs supported by the 0.15 raised in 2009. This proposal is expected to generate $1.4 billion in the budget year.

May Revision. The Governor has modified the realignment proposal to reduce the public safety programs being realigned by approximately $270 million. The Governor is therefore reducing the revenues dedicated to realignment commensurately. Instead of dedicating all 0.5 percent of the VLF, the Governor now proposes to dedicate 0.4 percent of the VLF to realignment and the remaining 0.1 percent to the General Fund to support schools. The Governor does not propose any changes to the Sales Tax extension.

Staff Recommendation. Staff recommends that the Subcommittee approve the May Revision proposal to modify the allocation of the VLF to reflect the revised realignment proposal.

Action: Approved staff recommendation on a 2 – 1 vote, with Senator La Malfa voting "no".

2. Maintain Existing Taxes: Education

Governor's Budget and 2011 Budget Conference Committee. The Governor's budget proposed a constitutional amendment maintaining the following tax rates for a five year period dedicated to education that will generate **$5.2 billion** annually. The 2011 Budget Conference Committee approved this measure in March of this year, as follows:

- **Maintain 0.25 percent Surcharge.** A PIT surcharge of 0.25 percent was enacted effective in the 2009 and 2010 tax years. The Governor's budget estimates that maintaining this surcharge would generate $3.3 billion in the current and budget years.
- **Maintain Reduced Dependent Exemption Credit.** The dependent exemption credit was reduced from $309 to $99 effective in the 2009 and 2010 tax years. The Governor's budget estimates that maintaining this reduced credit will generate about $2 billion in the current and budget years.

May Revision. The Governor has proposed to reduce the tax package proposed in January by eliminating the 0.25 percent surcharge for the 2011 tax year. The Governor does propose to reinstate the 2010 tax rate in the 2012 tax year for a four year period. This change reduces the tax package by $2 billion relative to the Governor's budget. The Governor does not propose any changes to the dependent credit proposal.

Staff Recommendation. Staff recommends that the Subcommittee approve the Governor's elimination of the 0.25 percent surcharge for the 2011 tax year.

Action: Approved staff recommendation on a 3 – 0 vote.

3. Targeted Tax Expenditures: Enterprise Zones

Background. Existing law provides special tax incentives for four kinds of geographically targeted economic development areas. These areas include enterprise zones, local agency military base recovery areas (LAMBRAs), manufacturing enhancement areas (MEAs), and targeted tax areas (TTAs). The tax incentives enjoyed by businesses located in these areas include accelerated depreciation, 100 percent net operating loss carryover, wage credits, and credits for sales tax on equipment purchased for use in the zone. There are some differences among the tax incentives provided for each area, but taxpayers generally have access to each form of preferable tax treatment.

The law currently limits the number of enterprise zones (42), LAMBRAs (8), MEAs (2) and TTAs (1). The Department of Housing and Community Development has designated 42 enterprise zones and 7 LAMBRAs as of December 15, 2010.

Employers within enterprise zones are allowed to claim a tax credit of 50 percent of the wages paid to a qualified employee in the first year, 40 percent in the second year, 30 percent in the third year, 20 percent in the fourth year, and 10 percent in the fifth year, up to 150 percent of the minimum wage. Qualified employees include individuals: (1) eligible for job training programs; (1) eligible for most social welfare programs; (3) economically disadvantaged; (4) dislocated workers; (5) disabled and eligible or enrolled in a state rehabilitation plan; (6) veteran; (7) ex-offender; and (8) member of a federally recognized Indian Tribe. Furthermore, existing law also allows enterprise zones to designate targeted employment areas (TEAs) to contain census tracts where 51 percent or more of individuals are considered low or moderate income. Any hire made out of a TEA can qualify the taxpayer in the enterprise zone for the hiring tax credit and TEAs can be drawn outside the borders of the enterprise zones.

The tax expenditures related to these zones cost the state approximately **$300 million** annually.

Governor's Budget and 2011 Budget Conference Committee. The Governor's budget proposed to repeal the state tax benefits allowed in the four kinds of geographically targeted economic development areas described above. The proposal would have eliminated all state tax benefits for both newly earned credits and deductions and for credits that had been earned in prior years, but have not been used. Local agencies would have the option of keeping their local incentives. This proposal would have generated additional revenues of **$924 million** in the current and budget years. The 2011 Budget Conference Committee also approved this proposal.

May Revision. The Governor's May Revision withdraws the January proposal to repeal the tax benefits for enterprise zones. Instead the Governor proposes to reform enterprise zone hiring credits so that credits are only available to firms which actually increase their level of employment. Under the new hiring credit the taxpayer would be eligible for a $5,000 credit for each incremental full-time equivalent employee that they hire. These credits would be allowed if claimed on the taxpayer's original return.

Furthermore, the May Revision proposal limits a practice known as "retro-vouchering" by not allowing any new vouchers to be granted for tax years prior to 2011 when the application for that voucher was made more than 30 days after the date that the employee first begins employment. The May Revision proposes to limit enterprise zone credits to a five year carry-forward period to ensure that the credit is encouraging relatively profitable businesses.

This proposal would generate additional revenues of **$93 million** in the current and budget years.

Good Goal, But Not a Core State Responsibility. The enterprise zone program was formed in 1984 to help draw investment into depressed rural and urban areas. While this is a good goal, it is not a core responsibility of state government and given the state's chronic budget deficits it is important that all state spending, including tax expenditures be scrutinized. Furthermore, the Governor has proposed a new option for local governments that want to continue to fund economic development activities. Specifically, the Governor has proposed a constitutional amendment to provide for 55 percent voter approval for limited tax increases and bonding against local revenues for economic development projects.

Current Program Not Proven Effective. In addition, the LAO and others have found that enterprise zone tax benefits have little to any impact on the creation of economic activity or employment in California. The LAO found that the program mainly seemed to shift economic activity from one zone to another within California without doing anything to grow economic activity. Furthermore, there is some evidence that benefits from the enterprise zone program go to taxpayers whose behavior has not been affected at all by the program, but instead by firms that specialize in finding businesses that could benefit from the program and offering to prepare the taxpayers tax return on a percent of benefit basis. In these cases it is clear that the taxpayer did not relocate their business because of the enterprise zone – since they had to be told of the tax benefit after they had already relocated.

Reform versus Elimination. Recently there have been significant efforts to make some reforms to the enterprise zone program. Specifically, SB 974 (Steinberg) from 2010 proposed to eliminate Targeted Employment Areas (TEAs) and stop the practice of retro-vouchering. As mentioned above, TEAs allow a taxpayer to qualify an employer for a tax credit not based on who they are, but based solely on residence within a zip code range listed on his or her employment records. Retro vouchering essentially allows taxpayers to gain tax credits for hiring decisions made in the past. Taxpayers often use the TEA criterion and the retro-vouchering to check payroll records and essentially "mine" the data for qualified employees and then file tax claims for refunds with the State.

Staff Comment: With the May Revision, the Governor is proposing to maintain, but reform, the enterprise zone program. The reformed program would become more focused on job creation, which is one of the highest priorities of the state at this time.

Staff Recommendation. Staff recommends that the Subcommittee take the following actions:

- Withdraw the proposal to eliminate all tax incentives in enterprise zones.
- Approve trailer bill language to reform enterprise zone hiring credits.

Action: Approved staff recommendation on a 2 – 1 vote, with Senator La Malfa voting "no".

4. Jobs Tax Credit Expansion

Background. As part of the February 2009 budget package, the Legislature adopted SB X3 15 (Calderon) that included provisions to incentivize small business job creation through a small-business hiring tax credit. The legislation allows a qualified employer to claim an income tax credit of $3,000 for each additional full-time employee hired by the employer during the taxable years 2009 and 2010. Unused credits may be carried forward by the taxpayer to reduce the tax liability over the following eight years. The total taxpayer benefits – and General Fund revenue loss – from the credits is capped at $400 million. The amount of credit is prorated if the employee works fewer than 12 months during the employer's tax year. The credit is only available to a business that has 20 or fewer employees on the first day of the taxable year. When SB X3 15 was adopted, the revenue estimates assumed most of the credits would be both claimed and used to offset tax liability in the short term – reducing State tax revenue in 2008-09 and 2009-10 by a total of $345 million. However, the Administration indicates only about $36 million in credits were used to offset revenue in 2008-09 and 2009-10.

May Revision. The Governor's May Revision proposes to expand the job credit to further stimulate small business job creation. The credit would be extended into the 2011 and 2012 tax years, the credit would be increased from $3,000 to $4,000 per new job created, and the credit would be available to more employers by expanding the definition of small business from 20 or fewer employees, to 50 or fewer employees. Other components of the tax credit would remain unchanged such as the cap of $400 million for the program. Since the credit was not fully allocated in the 2009 and 2010 tax years and would now be extended to 2011 and 2012 tax years, this proposal does result in addition General Fund revenue loss relative to the baseline forecast. The revenue loss in 2010-11 is estimated by the Department of Finance at $29 million and the revenue loss in 2011-12 is estimated at $65 million.

Related May Finance Letter for the BT&H Agency. The Governor is also proposing to augment the budget of the Business, Transportation and Housing Agency (BT&H Agency) by $279,000 General Fund to add one position and fund consulting services, to increase public awareness of the tax credit. The Administration did not provide the typical Finance Letter detail with this proposal that would explain the activities of the new state staff and the consultant.

Staff Comment: While not explicitly linked to other revenue proposals in proposed trailer bill language, this proposal is a new tax expenditure that would reduce General Fund revenues by an estimated $94 million through June 2012. This new tax expenditure program would be difficult to fund in this constrained budget environment unless the Governor's tax extensions and tax policy reforms are also adopted. New General Fund expenditures of $279,000 are proposed marketing the program, but public outreach could also be accomplished within existing state resources such as press officers and Agency Secretaries that could publicize the program with speeches to local chambers of commerce, press events, etc.

Staff Recommendation. Staff recommends that the Subcommittee take the following actions:

- Approve trailer bill language to expand the jobs credit.
- Reject the $279,000 General Fund at the BT&H Agency for marketing the program, and instead achieve improvements to public outreach with existing resources.

Action: Approved staff recommendation on a 3 – 0 vote.

5. Sales and Use Tax Exemption—Manufacturing Equipment

Background. For a ten-year period ending December 31, 2003, California law provided a partial (General Fund only) sales and use tax exemption for purchases of equipment and machinery by new manufacturers, and income and corporation tax credits for existing manufacturers' investments (MIC) in equipment. The sales and use tax exemption provided relief of payment of the state tax portion for purchases of qualifying property, and the income tax credit was equal to six percent of the amount paid for qualified property placed in service in California. New manufacturers could either receive the benefit of the exemption, or claim the income tax credit. However, existing manufacturers could only receive the benefit of the income tax credit. This sales and use tax exemption and income tax credit had a conditional sunset date that was triggered when manufacturing employment (as determined by the Employment Development Department) did not exceed manufacturing employment as of January 1, 1994 by more than 100,000 workers. On January 1, 2003, manufacturing employment was less than the 1994 number by over 10,000 workers, and therefore the MIC and partial sales tax exemption expired at the end of 2003.

May Revision. The Governor's May Revision proposes to provide a new partial sales and use tax exemption for qualified purchases by a taxpayer involved in manufacturing starting July 1, 2012 and ending July 1, 2016. This exemption is similar to the exemption in state law from 1994 until 2003, but has differential exemptions for existing and new manufacturers. It is intended to decrease the cost of doing business for manufacturing companies in an attempt to stimulate investment and employment in those industries and to attract and expand business activity in California. The proposed credit would provide a full 5-percent exemption of the General Fund sales and use tax for new start-up firms and a 1-percent exemption for existing firms. The State General Fund revenue loss from the proposal is estimated at $261 million in 2012-13, increasing slightly thereafter through 2015-16.

Linked to Other Revenues. The proposed sunset for the manufacturers' tax exemption of July 1, 2016, is linked to the date the temporary taxes would expire. The proposed trailer bill language would make the new tax expenditure contingent on voter approval of a proposition on a future statewide general election ballot related to the tax extensions. These tax extensions are the sales tax and Vehicle License Fee revenues dedicated to realignment (see also agenda issue #1) and the personal income tax revenues dedicated to education (see also agenda issue #2). While not explicitly linked in the proposed trailer bill language, the Governor's May Revision document indicates the manufacturers' credit is not affordable unless his proposal is adopted to make the single sales factor mandatory. Note, the single sales factor proposal was adopted by the Budget Conference Committee, and the Governor proposed no change in the May Revision.

Staff Comment: As indicated above, this proposal is a new tax expenditure that would reduce General Fund revenues by an estimated $261 million in 2012-13. This new tax expenditure program would be difficult to fund in this constrained budget environment unless the Governor's tax extensions and tax policy reforms are also adopted.

Staff Recommendation. Approve trailer bill language to create a new manufacturers' tax credit contingent on the maintenance of existing taxes.

Action: Approved staff recommendation on a 2 – 0 vote, with Senator Evans not voting.

Senate Budget and Fiscal Review—Mark Leno, Chair

SUBCOMMITTEE NO. 4 Agenda

Senator Michael J. Rubio, Chair
Senator Noreen Evans
Senator Doug LaMalfa

Thursday, May 26, 2011
10:00 a.m.
Room 112

Consultants: Brian Annis, Kris Kuzmich, and Seija Virtanen

AGENDA PART B

DEPARTMENTS TO BE HEARD

(Please See Detailed Agenda on Pages 2 and 3 for More Specific Listing and Order of Departments and Issues to Be Heard)

0510	Secretary for State and Consumer Services
0520	Secretary for Business, Transportation, and Housing
0840	State Controller
0845	Department of Insurance
0911	Citizens Redistricting Commission
0950	State Treasurer
1705	Fair Employment and Housing Commission
1730	Franchise Tax Board
1760	Department of General Services
2240	Department of Housing and Community Development
2400	Department of Managed Health Care
8820	Commission on the Status of Women
8860	Department of Finance
8885	State Mandates
8940	Military Department
8955	California Department of Veterans Affairs
9600	Debt Service General Obligation Bonds & Commercial Paper
9620	Cash Management and Budgetary Loans
9860	Capital Outlay Planning and Studies Funding
CS 3.91	Reductions in State Operations
CS 4.30	Lease Revenue Payment Adjustments
CS 13.25	Reorganizations and Consolidations

AGENDA – VOTE ONLY ITEMS

(Please see summary chart on Pages 4 and 5)

AGENDA – DISCUSSION / VOTE ITEMS

Issues Proposed for Vote Only:

	Issue	Amount	Fund Source	Staff Recommendation
	Treasurer's Office (0950)			
1	Budget Bill Language for Bond Issuance Costs	$0 and BBL	Not applicable	APPROVE
	Department of General Services (1760)			
1	California Institute for Women Walker Clinic and Infirmary Buildings Structural Retrofit Project Reappropriation	$5,951,000	Seismic Bonds	APPROVE
2	Office Building 10 Renovation Project Extension	$437,000	Lease-Revenue Bonds	APPROVE
3	California Department of Transportation District 3 Office Replacement Project Extension	$851,000	Lease-Revenue Bonds	APPROVE
4	Provisional Language, California Health Care Facility Construction Services	N/A	N/A	APPROVE, as specified
	Department of Housing and Community Development (2240)			
1	Community Development Block Grant Service Funding Adjustment	$1,100,000 shift to local assistance and (-) 10 positions	Federal Funds	APPROVE
2	Propositions 46 and 1C Liquidation Extension Building Equity and Growth in Neighborhoods	N/A	N/A	APPROVE
3	Liquidation Extension *Vega et al. v. Richard Mallory* Settlement	N/A	N/A	APPROVE
4	Federal Neighborhood Stabilization Program Round 3	$11,300,000	Federal Funds	APPROVE
	Department of Managed Health Care (2400)			
1	Federal Grant Funds	$3,900,000	Federal Funds	APPROVE
	Commission on State Mandates (8885)			
1	Conforming Changes for State Local Realignment	$0 and BBL	N/A	APPROVE
2	Savings Based on State Controller's April 30 Report	-$3,900,000 (savings)	GF	APPROVE
	Debt Service General Obligation Bonds & Commercial Paper (9600)			
1	May Revision: New Estimates of Bond Debt Service	-$267,000,000 (savings)	GF	APPROVE
	Cash Management and Budgetary Loans (9620)			
1	Intra-year Payment Deferrals / Cashflow Loans	-$50,000,000 (savings)	GF	APPROVE

Issues Proposed for Vote Only, Continued:

	Capital Outlay Planning and Studies Funding (9860)			
1	Unallocated Capital Outlay Budget Reduction	$500,000	GF	APPROVE
	Lease-Revenue Payment Adjustments (CS 4.30)			
1	Various Lease-Revenue Bond Debt Service Adjustments	$471,000 $4,047,000	GF Other Funds	APPROVE

Vote:

Issues Proposed for Vote Only – Issue Descriptions

STATE TREASURER (0950)

Department Overview: The State Treasurer's Office (STO), a constitutionally established office, provides banking services for state government with goals to minimize interest and service costs and to maximize yield on investments. The Treasurer is responsible for the custody of all monies and securities belonging to or held in trust by the state; investment of temporarily idle state monies; administration of the sale of state bonds, their redemption and interest payments; and payment of warrants drawn by the State Controller and other state agencies.

January Governor's Budget Overview: The Governor proposed expenditures of $27.4 million ($4.7 million GF) and 229.7 positions – an increase of $981,000 (a GF increase of $43,000) and no change in positions. The year-over-year budget increase is primarily a result of employee compensation adjustments.

March Budget: In the March budget package, the Legislature approved the Treasurer's budget as proposed by the Governor.

Issue 1 – Budget Bill Language for Bond Issuance Costs

Budget Request: In the Governor's May Revision, the Treasurer's Office requests new budget bill language that would allow a GF augmentation of up to $800,000 only if needed due to a cancelled bond sale. If bonds are sold at market, bond proceeds are used to pay advertising expenses and rating agency fees. In rare cases, bond sales have been cancelled after costs are incurred for advertising expenses and rating agency fees. In those cases, there is no timely mechanism for the Treasurer to obtain funding for these costs.

Staff Comment: The Treasurer is not requesting a budget augmentation, but rather language that would allow the Director of Finance to approve an augmentation of up to $800,000 only if necessary due to a cancelled bond sale. Any such approval by the Director of Finance would be followed by notification to the Joint Legislative Budget Committee.

Staff Recommendation: Approve the May Finance letter.

DEPARTMENT OF GENERAL SERVICES (1760)

Department Overview. The Department of General Services (DGS) provides management review and support services to state departments. The DGS is responsible for the planning, acquisition, design, construction, maintenance, and operation of the state's office space and properties. It is also responsible for the procurement of materials, data processing services, communication, transportation, printing, and security.

Budget Overview. The January Governor's Budget provides the DGS with 3,923.8 authorized positions and $1.1 billion ($5.5 million GF). This is a decrease of eight positions and $18.5 million. As a central service agency, the vast majority of DGS' budget is comprised of special fund and reimbursement revenue, received for services performed for other state departments and agencies.

Issue 1 – California Institute for Women Walker Clinic and Infirmary Buildings Structural Retrofit Project Reappropriation

Governor's Request. In an April Finance Letter, the Governor requests to reappropriate a total of $5.951 million (seismic bonds) of working drawing and construction funds for the structural retrofit of the Walker Clinic and Infirmary Buildings at the California Institute for Women, Corona (CIW).

2010-11 Budget. The 2010-11 Budget provided funding in the amount of $5.452 million for the construction phase of the CIW project; total estimated costs are $6.402 million, including $85,000 – study phase, $393,000 – preliminary plans, and $472,000 – working drawings.

Background. The CIW houses all custody levels of female inmates and functions as a reception/processing center for incoming female inmates. In addition to its large general population, CIW houses inmates with special needs such as pregnancy, psychiatric care, methadone, and medical problems. The Walker Clinic and Infirmary Buildings were assessed and found to be seismically deficient, placing inmates, staff, and visitors at risk in the event of an earthquake. This project consists of a "structural only" retrofit, whereby the majority of the work will be accomplished with minimum disruption to existing interior work space functions.

Working drawing funds were originally provided in 2007-08; construction funds were provided in 2010-11. The schedule for this project was delayed due to the Pooled Money Investment Board's December 2008 action freezing all disbursements from AB 55 loans (which in turn caused numerous project suspensions). The CIW project was subsequently reactivated and working drawings are substantially complete; however, some minor work remains outstanding. As a result, it will not be possible for DGS to proceed to bid for construction by June 30, 2011. Therefore, in order to complete the design and eliminate the risk of losing the availability of construction funds, DGS is requesting a one-year reappropriation of funds until June 30, 2012.

Staff Comment. This project has been in the design phase for over four years; DOF indicates that this project will proceed to the construction phase in 2011-12. Further, DOF has verified that there are no intersections between this project and the federal receiver or AB 900 prison construction program.

Staff Recommendation. Approve the April Finance letter.

Issue 2 – Office Building 10 Renovation Project Extension

Governor's Request. In an April Finance Letter, the Governor requests to extend by one year the encumbrance and liquidation period for $437,000 (lease-revenue bonds) in construction funds for the Building Office 10 Renovation project.

2010-11 Budget. The 2010-11 Budget extended by one year, until June 30, 2011, the liquidation period for $569,000 (lease-revenue bonds) for the construction phase of the Office Building 10 Renovation project. It was reported at that time that while the project was substantially complete, some minor work related to the floors in the building remained outstanding, necessitating the one-year extension.

Background. Office Building 10 is located at 721 Capitol Mall. Built in the 1950s, it is one of the oldest buildings located on this part of Capitol Mall. It is a six-story, 148,000 gross square foot building that was renovated from January 2006 through October 2007 and was accepted in December 2007. Prior to its renovation, Office Building 10 was occupied by the Department of Education for 31 years; the Department of Rehabilitation has occupied the building since October 2007. The 2010-11 extension allowed completion of post-construction work to correct first floor junction boxes and the surrounding flooring. The current extension request will accommodate completion of a number of accessibility and security items identified after occupancy, primarily related to the installation of security card readers for strategic points within the building. This work cannot be completed prior to expiration of the current liquidation period of June 30, 2011. Therefore, DGS requests a one-year extension of the liquidation period to complete the project.

Staff Comment. The Office Building 10 Renovation project is now three and half years from acceptance. In 2010-11, the liquidation period was extended by one year to allow for floor repairs. DGS is requesting an additional one year extension in 2011-12. Given that this project was accepted nearly three and a half years ago, a question can be raised about how the needed work could still be considered "post construction warranty work." The fund source is lease revenue bonds, and the use of those funds is for either the Office Building 10 project or debt service related to the project. DOF has indicated that it is more cost effective and efficient to use the existing construction contract for one more year to finish this work; letting a new contract would add time to the schedule to get the needed repairs done. Further, the tenant in the building is the Department of Rehabilitation, so the accessibility issues need to be resolved. Approximately $200,000 of the $437,000 available will be used for this work in 2011-12; the remaining funds will then go to debt service.

Staff Recommendation. Approve the April Finance letter.

Issue 3 – California Department of Transportation District 3 Office Replacement Project Extension

Governor's Request. In an April Finance Letter, the Governor requests to extend by one year the encumbrance and liquidation period for $851,000 (lease-revenue bonds) in construction funds for the California Department of Transportation District 3 Office, Marysville, Office Replacement project.

Background. Funds were originally provided in 2003-04, reappropriated in 2005-06 with an additional supplemental appropriation that year. These funds must be liquidated by June 30, 2011, or the authority will revert. Although construction is currently nearing completion, the project suffered a schedule delay due to the Pooled Money Investment Board's December 2008 action freezing all disbursements from AB 55 loans. As a result of this delay, DGS extended the construction completion date to April 15, 2011. However, DGS is still seeking Leadership in Energy & Environmental Design (LEED) certification and requires additional time to complete close-out activities related to contract acceptance. As a result, DGS requests a one-year extension of the liquidation period to complete the project.

Staff Recommendation. Approve the April Finance letter.

Issue 4 – Provisional Language, California Health Care Facility Construction Services

Governor's Request. In a May Revision Finance letter, the Governor requests to add provisional budget bill language that authorizes the DOF to augment DGS for additional workload costs related to construction inspection services for the California Health Care Facility (CHCF) project in Stockton.

Background. Funding for the CHCF project is pending approval by the State Public Works Board, thus the timing of the CHCF project is uncertain. Site construction is anticipated to begin in late 2011 or early 2012 and the facility will be staffed and occupied by December 2013. As a result of this uncertainty, the level of resources required to provide mandated inspection services is also unknown. This language will enable the DGS to request funding based on the timing of inspection services after project funding has been secured. It will also provide DOF time to review and approve resources requested and require notification to the Legislature.

Staff Comment. This provisional language is warranted. However, staff notes that the proposed language would allow DGS, with the prior written consent of DOF and based on any augmentation made in accordance with the provision, to potentially increase rates charged to other departments for services or the purchases of goods. Staff notes that no compelling case has been made as to why, under any circumstance, an augmentation under this provision would result in a DGS need to increase other departments' rates. Therefore, in considering this request, staff recommends that the following wording be removed from the proposed language:

1760-001-0602

1. (a) Notwithstanding Provisions 3 and 4 of Item 1760-001-0666, the Director of Finance may augment Item 1760-001-0602, when the State Public Works Board has approved the California Health Care Facility project in Stockton. Any augmentation that is deemed necessary on a permanent basis shall be submitted for review as part of the normal budget development process. Any augmentation made in accordance with this provision shall not result in an increase in any rate charged to other departments for services of the purchase of goods ~~without the prior written consent of the Director of Finance~~.
   (b) Any augmentation made pursuant to Section (a) of this provision shall be reported in writing to the chairpersons of the fiscal committees of each house of the Legislature and the Chairperson of the Joint Legislative Budget Committee within 30 days of the date the augmentation is approved. This notification shall be provided in a format consistent with normal budget change request, including identification of the amount of, and justification for, the augmentation, and the program that has been augmented.

Staff Recommendation. Approve the May Finance letter, as modified.

DEPARTMENT OF HOUSING AND COMMUNITY DEVELOPMENT (2240)

Department Overview. A primary objective of the Department of Housing and Community Development (HCD) is to expand housing opportunities for all Californians. The Department administers housing finance, economic development, and rehabilitation programs with emphasis on meeting the shelter needs of low-income persons and families, and other special needs groups. It also administers and implements building codes, manages mobilehome registration and titling, and enforces construction standards for mobilehomes.

Budget Overview. The January Governor's Budget provides the HCD 598.6 authorized positions and $256.0 million ($8.8 million GF). This is a decrease of 6.5 positions and $490.0 million. The majority of the HCD's expenditures are supported by general obligation bond revenue; the HCD's budget has been steadily decreasing in recent years due to the pending exhaustion of housing bond funds.

Issue 1 – Community Development Block Grant Service Funding Adjustment

Governor's Request. As part of the January budget, the Governor requests a shift of $1.1 million in federal budget authority from State Operations to Local Assistance and a reduction of ten positions for the Community Development Block Grant (CDBG) program to reflect a correction in federally allowable administrative costs. To accommodate the reduced level of program administration funding, HCD plans to make programmatic changes which are discussed further below.

Prior Subcommittee Action. This request was denied without prejudice at the Subcommittee's January 27, 2011 hearing, to allow time for the impacts of these proposed changes to be fully analyzed and determine if there were other approaches that could be developed that would have less programmatic impact on recipient communities.

Background. HCD's CDBG program was established over twenty-eight years ago to address the fact that California's non-entitlement jurisdictions, which are smaller communities (many of which are rural and economically distressed), lack the resources and/or economies of scale to receive, award, and monitor these federal grants in an efficient and effective manner that allocates the funds to the most pressing needs, meets all federal requirements, and protects against fraud. HCD's CDBG program currently serves 168 non-entitlement jurisdictions.

Although HCD has authority for 28 positions, the federal funding available is only sufficient to support 18 of those positions. The source of the current problem is a combination of short- and long-term factors and some recent issues regarding the funding for the HCD administration of the CDBG program, including: (1) the complexity and scope of the program makes it labor intensive to administer; (2) the federal allowance for state administration costs for the program is minimal; and, (3) the $1.1 million increase in the program budget in 2007-08, which included a shift of $697,000 CDBG program administration funding from GF to federal funds, cannot be sustained due to federal restrictions.

In response to concerns raised at the Subcommittee's January 27, 2011, hearing HCD worked with its CDBG Advisory Committee, comprised of a combination of CDBG jurisdictions, consultants, and non-profit organizations, to develop and finalize a set of new policies to ensure the broadest possible eligibility for local governments and the continued effective operation of this valuable federal resource, as follows:

1. Super NOFA – One combined Notification of Funding Availability (NOFA) to be released annually each January.
2. 50 Percent Rule – Jurisdictions with open contracts must expend 50 percent of their funds before being eligible for additional funding to encourage jurisdictions to spend the funds and increase the State's expenditure rate with federal Housing and Urban Development. This policy would also increase the number of jurisdictions that HCD funds as new jurisdictions will be coming in every other year for funding.
3. Funding Based on Demand – The amount of funds eligible for an activity would be determined by demand or regulatory minimum requirements.
4. Increased Maximums – Increase the maximum funding requests to $2 million (from $1 million) and increase the maximums on the activities. The biggest increase would be for the Public Improvement projects from $800,000 to $1.5 million. In HCD roundtables and committee meetings, it has been a common theme that jurisdictions want the ability to fund public improvement projects and that the current maximum was too low.
5. Limit of Three Activities per Application – A jurisdiction may be awarded one, two, three, or none depending on demand for each activity.

Staff Comment. The budgetary adjustment must be adopted due to federal requirements; the question of how it will be implemented and its impact on recipient communities raised concerns for the Subcommittee when this request was heard earlier this year. The revised implementation policies before the Subcommittee respond to those concerns and should ensure the broadest possible eligibility for the recipient communities.

Staff Recommendation: Approve the budget request.

Issue 2 – Propositions 46 and 1C Liquidation Extension Building Equity and Growth in Neighborhoods

Governor's Request. In a May Revision Finance letter, the Governor requests an extension of the liquidation dates for the three Building Equity and Growth in Neighborhoods (BEGIN) program Budget Act appropriations. The affected budget act appropriations and liquidation dates are for the 2005-06, 2006-07, and 2007-08 fiscal years. For the 2005-06 and 2006-07 appropriations, it is requested that the liquidation period be extended from June 30, 2011, to June 30, 2013. For the 2007-08 appropriations, it is requested that the liquidation period be extended from June 30, 2012 to June 30, 2013.

Background. The BEGIN programs make grants to qualifying cities, counties, or cities and counties to be used for down payment assistance to qualifying first-time home buyers of low and moderate incomes purchasing newly constructed homes in a BEGIN project. In order to qualify, an applicant city, county, or city and county must provide regulatory relief and fee reductions to developers. The Administration is seeking these liquidation extensions because while the applicant jurisdictions have provided the regulatory relief as required by the BEGIN awards, additional time is needed for liquidation to provide the time necessary to fulfill the final steps of the program obligations, complete projects, and find qualified homebuyers.

Staff Comment. While these appropriations were originally made in different years, the requested liquidation extensions are two years and one year, respectively. The Administration indicates this is to reduce administrative program costs by placing these appropriations on the same "cycle."

Staff Recommendation. Approve the May Finance letter.

Issue 3 – Liquidation Extension Vega et al. v. Richard Mallory Settlement

Governor's Request. In a May Revision Finance letter, the Governor requests an extension of the liquidation date until June 30, 2014, for the $601,000 GF appropriation provided by Chapter 163, Statutes of 2006, for the costs of settlement in the case of *Vega et al. v. Richard Mallory*, California Department of Housing and Community Development (Sacramento County Superior Court, Case No. 97AS06548).

Background. The HCD Office of Migrant Services (OMS) provides safe, decent, and affordable seasonal rental housing and support services for migrant farmworker families during the peak harvest season through grants to local government agencies that contract with HCD to operate OMS centers located throughout the state. HCD obtains and administers funds for the construction and rebuilding of OMS centers

Chapter 163 provided the final funding for HCD to complete the repayment process prescribed by the *Vega v. Mallory* Settlement, which addressed overcharges by the OMS to center residents. The settlement provides that any remaining funds, after payment of all center resident claims, be used for OMS center repairs. However, the term of liquidation under Chapter 163 will expire before HCD can complete the process to utilize the remaining funds for OMS center repairs.

HCD reports that the court-appointed third-party settlement administrator did not notify HCD of the last payment being made in time for HCD to begin the process, as stated in the settlement, to utilize the remaining funds for OMS center repairs. Nonetheless, failure to use those funds for that purpose would be a violation of the settlement agreement by the HCD. This request would provide an extension to June 30, 2014, which is enough time for the OMS program to complete the process required through the settlement agreement as well as the usual repair process used by the state, thereby satisfying the requirements of the *Vega v. Mallory* settlement.

Staff Recommendation. Approve the May Finance letter.

Issue 4 – Federal Neighborhood Stabilization Program: Round 3

Governor's Request. In a May Revision Finance letter, the Governor requests approval for an increase in the Federal Fund Loan Assistance budget act authority of $11.3 million (federal funds) for the Neighborhood Stabilization Program, Round 3 (NSP3), as authorized by the Wall Street Reform and Consumer Protection Act of 2010. No additional authority is requested for state operations because HCD is reassigning staff to address this workload for the next five years.

Background. The federal NSP program is intended to assist states and local governments in the redevelopment of abandoned and foreclosed residential properties. The federal Department of Housing and Urban Development developed a formula for distributing funds based on the highest need resulting from home foreclosures. California received $145 million in Round 1 funding; HCD subsequently allocated those funds for statewide distribution. In Round 2, California localities received $314 million; HCD did not receive any funds in Round 2. Round 3 funding was restricted to areas of greatest need. HCD applied for and was granted $11.3 million in Round 3 federal funds to continue to manage and distribute funds to assist in solving California's problems of blighted neighborhoods.

HCD is reserving $590,000 of the total grant award for program administrative costs over the next five years. No additional budget authority is needed to because HCD expects to reassign existing staff to address the NSP3 workload; the position assigned to NSP1, where workload is declining, will move to the NSP3 as workload there begins to increase in 2011-12.

Staff Recommendation: Approve the May Finance letter.

DEPARTMENT OF MANAGED HEALTH CARE (2400)

For overview and budget information regarding this department, please see page 30 of this agenda.

Issue 1 – Federal Grant Funds

Governor's Request. In a May Revision Finance letter, the governor requests a reappropriation of $3.9 million in federal grant funds for activities to raise consumer awareness about federal health care reform and the Patient Protection and Affordable Care Act.

Background. In January 2011, the Joint Legislative Budget Committee (JLBC) approved $4.2 million federal funds expenditure for the Department of Managed Health Care (DMHC) to perform education and outreach activities to raise consumer awareness about federal health care reform. Due to delays in executing contracts for the provision of outreach and education services, DMHC will be unable to expend the entirety of the grant funds in the current fiscal year. This request is to allow DMHC to expend the remainder of the funds during the 2011-12 fiscal year.

DMHC intends to expend the grant funds for website design and content, translation services to provide consumer friendly access, enhancement of the communications system with upgraded hardware, and creating an online grievance/Independent Medical Review application that permits the efficient handling of increased consumer calls and complaint cases.

Staff Recommendation: Approve the May Finance letter.

COMMISSION ON STATE MANDATES (8885)

Department Overview: The Commission on State Mandates (Commission) is responsible for determining whether a new statute, executive order, or regulation contains a reimbursable state mandate on local governments and determining the appropriate reimbursement to local governments from a mandate claim. This budget item appropriates the funding for the staff and operations costs of the Commission, and appropriates non-education mandate payments to local governments. The Constitution, as amended by Proposition 1A of 2004, requires that the Legislature either fund or suspend local mandates – in most cases, if the Legislature fails to fund a mandate, the legal requirements are considered suspended pursuant to the Constitution. Payments for mandate costs incurred prior to 2004 are one exception noted in the Constitution, as are mandates related to labor relations.

Governor's January Budget Overview: The January Governor's Budget proposed expenditures of $56.7 million ($53.7 million GF) and 11.0 positions, a decrease of about $27.9 million over the adjusted current-year budget and no change in positions. It should be noted, the 2010-11 adjusted funding level is after the prior Governor's veto of $131 million. The Governor's budget includes the continuation of certain mandate suspensions, some new mandate suspensions, and deferrals of mandate payments to generate GF savings of about $321.7 million. The savings measures include: (1) savings of $94.0 million by deferring payment of pre-2004 mandate claims; (2) savings of $172.6 million by suspending certain local mandates; and (3) savings of $55.1 million from deferring payment on expired mandates or some mandates exempt from the requirements of Proposition 1A of 2004. Under (2) above, most mandates are proposed for suspension except those related to law enforcement and tax collection. Generally, the Governor proposed to fund only mandates related to law enforcement and local property tax collection.

March Budget Package: In March, the Legislature adopted a budget for the Commission similar to that proposed by the Governor ($53.7 million GF). However, in adopting the revised realignment package, the Legislature included a costs offset in another budget item for local law enforcement mandates, because those costs would be covered from new realignment revenues. The realignment action resulted in technical changes to the Commission on State Mandates item where those law enforcement mandates were deleted from the list of funded mandates.

May Revision: The Governor's May Revision includes several adjustments to the Commission on State Mandates Budget that result in a net GF cost reduction of $3.9 million.

Issue 1 – Conforming Changes for State Local Realignment

Governor's Request: In the May Revision, the Governor has modified his local realignment proposal to remove the $50.9 million associated with law enforcement mandates. To technically conform to this proposal, the mandates budget item needs to be modified to again list all the law enforcement mandates. Due to how this was budgeted in March with offsetting savings in another budget item, the $50.9 million is currently built into the mandates budget item and no changes are required to the level of appropriation.

Staff Comment: The public safety realignment proposal is primarily in the venue of Budget Subcommittee #5. Any changes by subject matter to the realignment package should be properly reflected in the budget for the State Mandate Commission.

Staff Recommendation: Conform the mandates budget to the final realignment package.

Issue 2 – Savings Based on State Controller's April 30 Report

Governor's Request: In the May Revision, the Governor requests a funding reduction of $3.9 million GF to reflect a revised cost estimate for law enforcement and property tax mandate reimbursements.

Staff Comment: The January budget is built on estimates of mandate claims, and the April State Controller report is updated for actual claims.

Staff Recommendation: Approve the May Revision request.

DEBT SERVICE GENERAL OBLIGATION BONDS & COMMERCIAL PAPER (9600)

Department Overview: Debt service payments are continuously appropriated, and therefore not appropriated in the annual budget bill. This item in the Governor's Budget displays the estimated debt service costs for each General Obligation bond (GO bond). Some bond costs are offset by special funds or federal funds – primarily by the transportation debt service fund. Other bonds are "self-liquidating," or have their own dedicated revenue (i.e., the Economic Recovery Bonds [ERBs] receive a quarter-cent of the sales tax) – the self-liquidating bonds are not included in this item.

January Governor's Budget Overview: The January Governor's Budget includes $4.9 billion in General Fund costs for GO debt service and related costs. In addition to this amount, $792 million in debt costs are funded from other funds (i.e., $778 million is from the Transportation Debt Services Fund that is associated with the truck-weight-fee proposal). Finally, federal bond subsidies, through the Build America Bonds (BABs) program, provide $351 million in 2011-12. The table below, with data from the January Governor's Budget, shows the three-year GO bond costs (in millions):

	2009-10 Actual Cost	**2010-11 Estimated Cost**	**2011-12 Estimated Cost**
General Fund cost	$4,639	$4,890	$4,927
Other funds cost	$239	$644	$792
Federal subsidy (Build America Bond Program)	$155	$300	$351
TOTAL Item 9600	**$5,033**	**$5,834**	**$6,070**
Economic Recovery Bonds (not included above)	$1,566	$1,351	$1,407

(see issue on next page)

Issue 1 – May Revision: New Estimates of Bond Debt Service

Governor's Proposal: As indicated above, funds for bond debt service are continuously appropriated and are considered one of the highest priorities for state expenditures. The Administration has new estimates for the cost of debt service in 2010-11 and 2011-12 that result in General Fund cost savings that total $267 million. One reason for the 2011-12 savings is that the Administration proposes to reduce its Fall 2011 bond sales from $5.8 billion to $1.5 billion. The Administration indicates that as of April 2011, total cash of $10.8 billion remains from prior bond issuances. So the new bond issuance of $1.5 billion would be sufficient to continue the bond program until a Spring 2012 issuance. The table below, with data from the Governor's Budget and May Revision, shows the three-year GO bond costs (in millions):

	2009-10 Actual Cost	**2010-11 Estimated Cost**	**2011-12 Estimated Cost**
January Budget General Fund cost	$4,639	$4,890	$4,927
May Revision Budget Adjustment	$0	-$140	-$126
Final Estimate of Cost	**$4,639**	**$4,749**	**$4,800**

Staff Recommendation: Approve the Administration's new cost estimate for GO bond debt service.

CASH MANAGEMENT AND BUDGETARY LOANS (9620)

Department Overview: This budget item appropriates funds to pay interest costs on General Fund borrowing used to overcome cash flow imbalances during the fiscal year. Because receipts and disbursements occur unevenly throughout the fiscal year, the General Fund borrows in most years, even though each budget is balanced when enacted and funds are repaid within the fiscal year. Interest is paid on both internal borrowing (such as cashflow loans from special funds) and for external borrowing (such as Revenue Anticipation Notes [RANs]). This item additionally pays interest costs for budgetary borrowing by the General Fund from special funds. Budgetary borrowing is across fiscal years and is scored as a budget solution, whereas cashflow borrowing is not counted as a budget solution (only a cash solution).

January Governor's Budget Overview: The January Governor's Budget included $300 million for interest costs on cashflow borrowing and $62 million for interest costs on budgetary borrowing – all General Fund. Of the cashflow amount, $100 million is for internal borrowing and $200 million is for external borrowing. Overall, expenditures in this item are up significantly – a total of $362 million is proposed for 2011-12, versus revised expenditures of $230 million in 2010-11. The year-over-year difference is primarily explained by the late budget last year that delayed the RAN sale until late in 2010. The Administration assumes the 2011-12 RAN sale will occur in July, resulting in a longer borrowing period and higher interest costs.

March Budget Action: The Legislature approved most of the Governor's cost assumption in the March budget package. An exception was that interest costs for special fund budgetary loans were reduced from $62.0 million to $57.7 million due to related budget action on special fund loans.

Issue 1 – Intra-year Payment Deferrals / Cashflow Loans

Governor's Proposal: The Administration has new estimates for the interest cost on special fund cashflow loans. The cost estimate is revised down from $100 million to $75 million in both 2010-11 and 2011-12. Estimated total GF savings over the two years totals $50 million.

Staff Recommendation: Approve the Administration's new cost estimates for special fund cashflow loans.

CAPITAL OUTLAY PLANNING AND STUDIES FUNDING (9860)

Issue 1 – Unallocated Capital Outlay Budget Reduction

Governor's Request. In a May Revision Finance letter, the Governor requests a decrease of $500,000 GF to reflect the reduction of the Unallocated Capital Outlay budget.

Background. The Unallocated Capital Outlay Budget provides funding to state agencies to develop design and cost information for new projects, known as "budget packages." The January Governor's Budget included $500,000 for these purposes in 2011-12. In prior years, the total funding provided was $1 million. This request would effectively zero out these funds in 2011-12.

Due to the current fiscal condition of the state, fewer infrastructure projects are being authorized and, as such, the state is preparing fewer budget packages. As a result, the Administration has determined that the $500,000 budgeted for 2011-12 is not needed because there are sufficient funds remaining for carryover from the 2010-11 appropriation. To the extent that it is determined that funds for budget packages are needed in 2012-13, it is anticipated that a request will be submitted through the normal budget process.

Staff Recommendation: Approve the May Finance letter.

LEASE REVENUE PAYMENT ADJUSTMENTS (CS 4.30)

Issue 1 – Various Lease-Revenue Bond Debt Service Adjustments

Governor's Request. In a May Revision Finance letter, the Governor requests various technical adjustments to amounts budgeted for lease-revenue debt service payments in 2011-12. The total of these changes is a decrease of $471,000 GF and a decrease of $4.047 million (other funds).

Background. Control Section 4.30 authorizes the Director of Finance to adjust amounts in appropriation items for rental payments on lease-purchase and lease-revenue bonds. In the case of the budgeted amounts for lease-revenue bond debt service in 2011-12, the decreases to the budgeted debt service amounts are a result of an update in the estimates of when bonds will be able to be sold.

Staff Recommendation: Approve the May Finance letter.

0840 STATE CONTROLLER

Department Overview. The State Controller is the Chief Fiscal Officer of the state. The primary functions of the State Controller's Office (SCO) are to provide sound fiscal control over both receipts and disbursements of public funds; to report periodically on the financial operations and condition of both state and local government; to make certain that money due the state is collected through fair, equitable, and effective tax administration; to provide fiscal guidance to local governments; to serve as a member of numerous policy-making state boards and commissions; and, to administer the Unclaimed Property and Property Tax Postponement Programs.

Budget Overview. The January Governor's Budget provides the SCO with 1,491 authorized positions and $218.9 million ($76.5 million GF). This is an increase of two positions and $65,000.

Issues Proposed for Discussion / Vote

Issue 1 – Local Government Oversight Initiative (April Finance Letter and May Revision Finance Letter)

Governor's Request. In an April Finance Letter, the Governor requests increased expenditure authority of $2.098 million (reimbursements) to support 16.4 existing positions to provide increased oversight of local government entities under the SCO's existing statutory authority.

In a separate May Revision Finance letter, the Governor requests increased expenditure authority of $1.44 million (GF) and ongoing to support 11.8 positions for increased oversight of local government entities under the SCO's existing and proposed statutory authorities.

Prior Subcommittee Action. The April Finance letter was held open at the Subcommittee's May 5, 2011, hearing, pending receipt of a systematic plan from the SCO detailing how the SCO would execute the additional activities, as well as an audit plan and a benefit/cost assessment of the additional financial monitoring.

Background. Generally speaking, direct state oversight of local governments is currently limited to state and federal pass-through funding. Counties receive a large share of state/federal pass-through funding to administer a number of statewide programs under state supervision, such as health and welfare. As a result, they receive direct state oversight, including SCO audits. For cities and special districts, state oversight is more limited to the few grants or allocations of state/federal pass through funding, such as Gas Tax allocations, distributed by the state. In addition, current statute provides for a more indirect oversight of local government funding using the following three elements:

1. <u>Annual Audits</u>. Each local government entity is required to have an annual audit performed by an independent auditor. If the local government has over $500,000 in federal expenditures, it must also have a single audit. Local governments are required to submit these single audits to the SCO.
2. <u>Financial Transaction Reports</u>. Statute requires the SCO to collect a report of annual financial transactions from each county, city, and special district and to publish them in

reports available to the Governor, legislature, and general public. Statute further provides that, if the reports are not made in the time, form, and manner required, or if there is reason to believe a report is false, incomplete, or incorrect, the SCO shall appoint a qualified accountant to make an investigation and to obtain the information required. Statute specifies that the SCO's enforcement costs are to be reimbursed by the local government entity in question. Statute also specifies that the Controller can impose financial penalties for late filing (or failure to file) of a financial transaction report by a local government entity. The penalties range from $1,000 to $5,000, dependent the total revenue of the government entity. On average, approximately $251,000 in such penalties is invoiced each year with approximately $100,000 received, which is then deposited into the GF.

3. Accounting and Audit Guidelines. Uniform accounting guidelines are intended to provide local governments with the information necessary to implement and operate a common accounting and reporting system. Currently such guidelines are only required for counties and special districts.

With regard to the financial transaction reports, these reports represent the only source of available statewide financial data on local government entities. According to 2010 estimates, the SCO staff spent more than 1,100 hours annually on monitoring the submissions and collecting forfeitures (required payments to the state for failure to file the financial report with the SCO). The SCO indicates that the reports are subject to automated edits that do not necessarily identify all the issues that warrant attention. For instance, the SCO does not presently have the resources to compare these reports between years or between similar entities. In addition, the current analyses of all of the complaints that are being submitted to the SCO (since the City of Bell stories were reported last year) are being done through staff redirections. To the extent that an analysis results in a need for further investigation, additional redirections would be needed.

Staff Comment. The current approach is not working at an optimal level to protect taxpayers from waste, fraud, and abusive financial practices. In response, the SCO has developed a Local Government Oversight Initiative, which is intended to increase oversight of local government financial matters. There is merit in increasing oversight, as most state money is spent at the local level.

As noted above, the SCO's initiative is presented in two requests. The April Finance letter consists of using the SCO's existing statutory authority to expand oversight and utilizing reimbursements from local governments to fund the SCO's costs. More specifically, this request would rely on increased expenditure authority of $2.1 million (reimbursements) to support 16.4 positions on an ongoing basis. This request focuses on the financial transaction reports detailed above and would provide resources to the SCO to investigate and prepare annual financial transaction reports for all non-filers, as well as conduct investigations of individual financial issues that indicate some information in an annual transaction report is "false, incorrect, or incomplete." However, as noted in the SCO's submitted audit plan, "the only way to determine the precise level of workload is to actually perform it." This raises questions about the long-term level of workload, as well as whether the SCO will be able to secure sufficient reimbursements. Failure to secure sufficient reimbursements would put the GF at risk for being the fund source to support these activities. Therefore, in considering this request, the Subcommittee may wish to: (1) reduce the resources by half; (2) make the approval three-year limited-term; and (3) adopt placeholder supplemental report language to require an annual report documenting the level of effort and findings and outcomes, to ensure that the

Subcommittee has a future opportunity to revisit this initiative and ensure desired outcomes are being achieved.

With regard to the May Revision Finance letter, this request proposes a mix of current and proposed statutory authority (the SCO is sponsoring two pending bills) to increase oversight by: (1) increasing the types of audits of local government that are submitted to the SCO; (2) increasing the number of quality control reviews of audits of local government; (3) posting all local government audits to, and establishing a "dashboard" of information on each city, county, and special district on, the SCO's website; (3) increasing the current penalties for failure to file annual transaction reports; and (4) expanding the collection and reporting of local government compensation data to include all local government entities. This request would rely on new GF spending of $1.44 million to support 11.8 positions on an ongoing basis. As noted above, it is not clear that the workload here is ongoing and sustainable. Further, the SCO is sponsoring two bills, AB 229 (Lara) and AB 276 (Alejo), to make the statutory changes necessary for the SCO to carry out the new duties under this request as well as increase the penalties. As such, and in considering this request, the Subcommittee may wish to defer to the policy process and then consider any requests to further expand the SCO's local government oversight activities once the bill process has concluded and as part of the 2012-13 budget process in January of next year.

Staff Recommendation:

- **April Finance letter**: Approve the April Finance letter as modified: (1) three-year limited-term basis $1.049 million (reimbursements) to support 8.2 existing positions and (2) placeholder supplemental report language requiring the SCO to report annually on its level of effort and findings and outcomes related to increased oversight of local government finances.

- **May Finance letter**: Reject the May Finance Letter and defer to legislative policy process.

Vote:

Issue 2 – Unclaimed Property Holder Compliance Initiative

Governor's Request. In a May Revision Finance letter, the Governor requests increased expenditure authority of $2.414 million (Unclaimed Property Fund - UPF) and 22.6 positions for 2011-12 ($2.442 million and 23.6 positions in 2012-13; $2.438 million and 23.6 positions in 2013-14 and ongoing) to develop and implement a holder outreach and compliance program to identify and contact non-reporters or inconsistent reporters of unclaimed property and bring them into compliance with the Unclaimed Property Law.

Related 2011-12 Budget Action. As part of the March 2011 Budget package, the Legislature approved the following related to the Unclaimed Property Program: (1) $293,000 (UPF), one permanent and 3.1 two-year limited term positions, for support of increased accounting workload; and (2) a two-year augmentation of $300,000 (UPF) for unclaimed property legal costs.

Background. Under the Unclaimed Property Law (UPL), the SCO is responsible for safeguarding unclaimed property until it is returned to its rightful owner. The UPL was enacted to ensure that property is returned to its rightful owner(s) and to prevent holders of unclaimed property from transferring it into their business income. Holders of unclaimed property must report and remit unclaimed property to the SCO after a specified period of time. In 2009, the SCO Division of Audits issued its first ever comprehensive analysis of holder compliance with the UPL by using Franchise Tax Board audits. The analysis identified 1.3 million active California-based businesses, of which at least 1,238,000 did not file an unclaimed property report with the SCO. The SCO believes that 34.5 percent of those filers are not required to file; of the remaining 851,000 businesses the SCO currently only receives 17,000 reports on an annual basis for a compliance rate of two percent. The SCO presents that a larger holder outreach unit would allow the SCO to contact non-compliant entities to bring them into compliance with the UPL. Of the 22.6 positions requested, 5.3 would be for outreach activities.

The SCO is also requesting to expand the audit activities under the Program, including desk reviews of businesses that have been audited to ensure they are still reporting on a yearly basis, and desk reviews of other businesses that have reported in the past to ensure they are reporting consistently. Of the 22.6 positions requested, 17.3 would be for audit activities.

The SCO estimates that this initiative will reunite owners with an estimated $113 million of their property over the next five years. Over the same five-year period, the increased efforts will result in remittance of approximately $136 million to be held in perpetuity for owners to claim. The SCO indicates that its initiative is self-funded and is estimated to result in net receipts to the GF in 2011-12 of $16.8 million, including $9.7 million from holder penalty and interest.

Staff Comment. In prior years, the SCO performed approximately 50 audits per year of unclaimed property holders within California. That audit work was reduced due to a budget reduction to the Unclaimed Property Program. To absorb those reductions, the SCO focused on work to return property to its rightful owner(s), as that is the goal of the program. Without an audit presence, the risks to holders for non-compliance diminish.

Staff Recommendation: Approve the May Finance letter.

Vote:

0845 DEPARTMENT OF INSURANCE

Department Overview. The California Department of Insurance (CDI) regulates the California insurance market and enforces the California Insurance Code, conducting examinations and investigations of insurance companies and producers and working to ensure the financial solvency of companies so that they will meet their obligations to policyholders and claimants. CDI investigates more than 300,000 complaints annually and responds to consumer inquiries. CDI also reviews and approves insurance rates to enforce the statutory requirement that rates are not excessive or unfair. CDI also administers the conservation and liquidation of insolvent and delinquent insurance companies and fights insurance fraud in conjunction with local and state law enforcement agencies.

Budget Overview. The January Governor's Budget provides CDI with 1,338 authorized positions and $224.94 million (Insurance Fund and reimbursements). This is an increase of 71 positions and $16.4 million.

Issue Proposed for Discussion / Vote

Issue 1 – Federal Health Care Reform: Additional 2011-12 Positions

Governor's Request. In a May Revision Finance letter, the Governor requests an increase of $748,000 (Insurance Fund) ongoing for eight existing positions to address the increased workload associated with defining and implementing federal health care reform (Patient Protection and Affordable Care Act – PPACA).

Prior 2011-12 Budget Actions. The Legislature approved earlier this year, as part of the March budget package, a total of 71 positions and $9.8 million (Insurance Fund) for the CDI, as follows:

2011-12 Funds	Positions	Function	Chapter Citation
$1,200,000	10 (9 2-year limited term and 1 1-year limited term)	PPACA and additional workload associated with the review of health insurance rate filings.	Chapter 661, Stats of 2010 (SB 1163)
$642,000	6 staff counsel, all 2-year limited-term	PPACA, additional rate filings, and new cancellation and non-renewal appeal process.	Chapter 658, Stats of 2010 (AB 2470)
$107,000	1 staff counsel, 2-year limited-term	PPACA and additional policy form review activities required as a result of the implementation of the California Health Benefits Exchange.	Chapters 659 and 655, Stats of 2010 (SB 900 and AB 1602, respectively)
$8,000,000	54 positions, permanent	Increased workload and to meet statutory mandates.	No change in statute cited.

Background. On March 23, 2010, President Obama signed the PPACA into law, a comprehensive health reform proposal intended to expand coverage, control health care costs, and improve the health care delivery system. The PPACA makes several fundamental changes to the private health insurance market, including setting up a new competitive private health insurance market through state Exchanges beginning in 2014, and prohibitions on lifetime benefit coverage limits and rescissions of coverage. In 2010, several state statutory changes were enacted to align California law with the new federal mandates under the PPACA. These statutory changes drove the 2011-12 budget requests summarized in the above chart.

The CDI requests these additional resources to implement PPACA for the following purposes: (1) providing expertise and consultation regarding legal and implementation issues to various CDI units; (2) legal consultation regarding proposed legislation; and (3) implementation of new legislation, policy monitoring, analysis, and recommendation regarding current and future impacts of health reform on CDI. Additionally, there will be workload associated with the coordination of future implementation activities with the Legislature, the Governor, the U.S. Department of Health and Human Services, and the National Association of Insurance Commissioners (NAIC), as well as mandated reporting requirements. The positions requested are as follows:

Positions	Classification	Funding
1.0	Associate Health Program Advisor	78,000
2.0	Health Program Specialist I	173,000
1.0	Health Program Specialist II	96,000
4.0	Staff Counsel	401,000
	TOTAL	**748,000**

LAO Recommendation. We recommend the Legislature reject the May Revision request for $748,000 in special funds to pay for eight currently authorized positions. Our analysis finds that the department has funding for 17 staff that is in excess of the level of resources justified on a workload basis. The department can redirect funds to pay for the eight positions.

Staff Comment. Unlike the regulatory adoption process here in California, PPACA devolved certain responsibilities for the regulatory process to the NAIC. Therefore, staff concurs that it is critical for the California Insurance Commissioner and key staff representatives to participate in NAIC activities related to the development of model laws and regulations for PPACA.

However, while the function of the eight positions being requested here is different from the Subcommittee's prior 2011-12 actions, these positions are proposed as permanent whereas the 17 PPACA-positions already approved are all limited-term. In discussions with staff, the CDI could not provide a clear explanation as to why these eight positions are proposed as permanent. In addition, post Subcommittee approval of the 54 position request earlier this year, the LAO was able to finalize its workload analysis of that request. The analysis found that of the 54 positions approved, 17 positions were unjustified.

Therefore, in considering this request, the Subcommittee may wish to consider not approving the request for increased expenditure authority and instead direct the CDI to absorb the workload within the January budget request. With 17 of those 54 positions determined to not be justified by the workload, there is ample capacity to absorb the workload in this May Revision request.

In either case, the Subcommittee may also wish to make any action here approved on a two-year limited-term basis, to ensure that all positions at CDI related to PPACA “cycle off” in two years' time to allow a full review of the workload and ensure the appropriate budget resources are provided. This is especially important because the full extent of the workload related to PPACA and changes in statute is not fully known.

Staff Recommendation: Deny the request for increased expenditure authority, and instead direct the Department of Insurance to absorb the workload in this request within the previously approved 54 positions.

Vote:

0911 CITIZENS REDISTRICTING COMMISSION

Issue Proposed for Discussion / Vote

Issue 1 – Citizens Redistricting Commission Continuing Activities

Governor's Request. In a May Revision Finance letter, the Governor requests that $400,000 GF be added to the 2011-12 budget to provide additional resources necessary for the Citizens Redistricting Commission (Commission) to complete the required redistricting maps by the constitutional deadline of August 15, 2011, and to perform related support activities. In addition, the Governor requests that provisional budget bill language be added to allow the Commission access of up to $1.5 million GF for litigation support activities in 2011-12.

Background. Proposition 11, the Voters FIRST Act, was approved by the voters on the November 4, 2008, General Election Ballot. Proposition 11 changed the state's redistricting process by establishing a 14-member Citizens Redistricting Commission (Commission) to draw the new district boundaries for the State Assembly, State Senate, and Board of Equalization beginning with the 2010 Census and every ten years thereafter. Proposition 11 specifies that a minimum of $3 million in funding be provided, or the amount appropriated for the previous redistricting plus the Consumer Price Index, whichever is greater.

Per the requirements of Proposition 11, the 2009-10 Budget appropriated $3 million GF for Proposition 11 implementation costs over a three-year period for the Commission, State Auditor, and Secretary of State. Additionally, the 2010-11 budget included provisional budget bill language to provide an expedited request process should the Commission demonstrate it required funding greater than the $2.5 million (amount that remained from the 2009-10 $3 million GF appropriation) for its costs from January 1, 2011, to June 30, 2011.

Proposition 20 was approved by the voters on the November 2, 2010 General Election Ballot, requiring changes and expansions to the 2008 amendments to the California Constitution. The 2010 amendments added California's 53 Congressional Districts to the Commission's redistricting responsibilities and expanded the criteria for the district mapping process. The amendments also shortened the completion date for all four maps and supporting reports to no later than August 15, 2011, thereby reducing the time allowed for the Commission's mandatory submission of the four maps to the Secretary of State by one month. These amendments were made with no additional appropriation of funds to support the expanded responsibilities and requirements.

In May 2011, the Joint Legislative Budget Committee approved the $1 million GF available through the 2010-11 budget provisional language. The Commission reports that it will have expended the entirety of the available funds by the end of 2010-11.

Staff Comment. The Commission has made a compelling case for the need for additional funds in the amount of $400,000 GF to complete its mandated work by the August 15, 2011, deadline. The proposed provisional budget bill language is similar to the approach taken in 2010-11, whereby there were some unknowns about the Commission's workload but a need for the Commission to have an expedited process and access to additional funds upon demonstrated need. At this point, it is not certain that litigation will be filed challenging the certified maps, but it would be wise to plan for that contingency. However, it is also important to not over appropriate this budget item; under the terms of Proposition 11, the total funding provided to this item creates a permanent baseline GF funding amount adjusted for inflation in future years. The Administration's May Revision proposal strikes the right balance to ensure this effort is appropriately and adequately funded.

Staff Recommendation: Approve the May Finance letter.

Vote:

2400 DEPARTMENT OF MANAGED HEALTH CARE

Department Overview. The Department of Managed Health Care (DMHC) was established in 2000, when the licensure and regulation of the managed health care industry was removed from the Department of Corporations and placed in a new, stand-alone, department. The mission of DMHC is to regulate, and provide quality-of-care and fiscal oversight for Health Maintenance Organizations (HMOs) and two Preferred Provider Organizations (PPOs). These 94 Health Care Plans provide health insurance coverage to approximately 64 percent of all Californians. Recent statutory changes also make DMHC responsible for the oversight of 240 Risk Bearing Organizations (RBOs), who actually deliver or manage a large proportion of the health care services provided to consumers. Within the Department, the Office of the Patient Advocate helps educate consumers about their HMO rights and responsibilities.

Budget Overview. The January Governor's Budget provides DFI with 250.2 authorized positions and $35 million (no GF). This is an increase of 2.7 positions and $55,000 over 2010-11.

Issue Proposed for Discussion / Vote

Issue 1 – Consumer Participation Program Sunset

Governor's Request. The Governor has no request.

Background. The Consumer Participation Program is housed within DMHC. Under this program, the DMHC Director may award advocacy and witness fees to a person or organization which represents the interests of consumers and has made a substantial contribution on their behalf to the adoption of a regulation, Director's order or decision affecting a significant number of consumers. The Director may identify regulatory proceedings in which he or she believes consumer participation would be helpful and anticipates that fees may be awarded. A person or organization desiring to participate in a proceeding and seek an award of fees will submit a *Petition to Participate in a Proceeding*. Current statute sets the total amount of compensation annually at $350,000. Similar programs currently exist at the Public Utilities Commission and at the Department of Insurance.

Staff Comment. It is important to note that the organizations receiving compensation are not being paid to advocate for consumers, they are being paid to inform the rulemaking process and to represent the experience of consumers with regard to what they have learned as they advocate.

Staff Recommendation: Approve trailer bill language to extend the Consumer Participation Program sunset until January 1, 2018.

Vote:

8885 STATE MANDATES

For additional background on the Commissions on State Mandates, including their total budget, please see the write-up in the vote-only section of the agenda.

Issues Proposed for Discussion / Vote

Issue 1 – Local Agency Formation Committees (LAFCO) Mandate

Governor's Request: In the May Revision, the Administration proposes: (1) to increase budget funding by $277,000 GF to reflect recent action by the Commission on State Mandates to adopt cost estimates for the LAFCO mandate; and (2) to suspend the LAFCO mandate and delete funding of $277,000 (payment would still be due in a future year) . The "LAFCO mandate" is a small part of LAFCO law – specifically, the requirement that special districts file written statement to LAFCOs specifying the functions of classes of service proved by those districts.

Constitutional Requirements: Proposition 1A of 2004 amended Section 6 of Article XIII B of the State Constitution to require that reimbursement claims from local governments either be paid, or that the mandate be suspended or repealed. So the State must either pay the LAFCO mandate in this budget, or suspend or repeal the requirements for 2011-12 to defer payment of the $277,000.

LAO Recommendation: The LAO recommends the Legislature adopt trailer bill language that would have the technical effect of repealing the LAFCO mandate. Repeal would simply *authorize*, instead of *require*, LAFCOs to direct special districts to file these statements. Since LAFCOs could still require the special districts to report, overall effect on the program should be none or minor. Other requirements of the LAFCO program would remain unchanged. With the LAO recommendation, the state would not have to pay the cost of this activity in future years, but the State will eventually have to pay the $277,000 for past claims.

Staff Recommendation: Approve the LAO trailer bill language.

Vote:

Issue 2 – Local Government Employment Relations Mandate

Governor's Request: In the May Revision, the Governor proposes: (1) to increase budget funding by $4.9 million GF to reflect recent action by the Commission on State Mandates to adopt cost estimates for the LGEF mandate; and (2) to defer payment of the LGEF mandate and delete funding of $4.9 million (payment would still be due in a future year). This mandate requires local governments to respond to charges of unfair labor practices made to the Public Employment Relations Board and deduct union dues from certain employees' paychecks.

Constitutional Requirements: Proposition 1A of 2004 amended Section 6 of Article XIII B of the State Constitution to require that reimbursement claims from local governments either be paid, or that the mandate be suspended or repealed. However, labor-relations mandates are specifically excluded from this requirement and payment can be deferred without suspension or repeal of the mandate. The Governor's proposal is to defer payment of the $4.9 million General Fund to an unspecified out-year and to keep the mandate requirements on local governments in place.

LAO Recommendation: The LAO recommends approval of the Governor's proposal to defer payment of the mandate. The LAO notes that the implementing legislation did not anticipate these State costs, and that in light of this, the relevant policy committee should again review these requirements.

Staff Recommendation: Approve the May Revision request.

Vote:

8940 MILITARY DEPARTMENT

Department Overview. The California Military Department (CMD) is responsible for the command, leadership, and management of the California Army and Air National Guard and five other related programs. The CMD is organized in accordance with federal Departments of the Army and Air Force staffing patterns. In addition to the funding that flows through the State Treasury, the CMD also receives Federal Funding directly from the Department of Defense.

Budget Overview. The January Governor's Budget provides the CMD with 854.5 authorized positions and $144.3 million ($46.0 million GF). This is a decrease of 11.0 positions and an increase of $3.8 million ($1.1 million GF).

Issue Proposed for Discussion / Vote

Issue 1 – Reduce Military Retirement Program

Governor's Request. In a May Revision Finance letter, the Governor requests a decrease of $1.5 million GF and two positions to reflect a reduction in retirement benefit costs provided to eligible retired service members. The CMD has since requested to maintain $300,000 of that savings and the two positions for an expansion of the California Cadet Corps.

Background. The CMD's Retirement Program (Program 40) was established prior to the CMD's participation in the California Public Employees Retirement System (CalPERS). Program 40 provides services similar to those provided by the federal military, to persons who entered State Active Duty (SAD) prior to October 1, 1961, and have served 20 or more years, at least 10 of which have been on SAD, or have been separated for physical disability. All other permanent civil service employees have been and are covered by CalPERS. Program 40 currently provides coverage for 29 individuals (12 retirees and 17 survivors of retirees).

The CMD indicates that when the SAD personnel hired after October 1, 1961, entered PERS, the monthly payroll was done as a manual hand-typed payroll submitted to the State Controller's Office (SCO). The CMD was responsible for calculating pay and all employer costs. When the checks were received from the SCO, the CMD was responsible for releasing the warrants for CalPERS, taxes, medical, Social Security, and Medicare. At the time, the SCO did not have a system that could calculate the military pay. In the 1990's, the CMD and the SCO were finally able to get the SAD personnel on the SCO payroll system. The retirement payroll in Program 40, which also was, and still is, a manual system done by the CMD, was not combined due to the fact that the employees on this payroll never paid into CalPERS and the SCO does not have a system that would enable the CMD to transfer this manual payroll. As the direct costs for Program 40 have gone down over the years due to retiree and or survivor deaths, the distributed portion of the program has not been reduced or reallocated to other programs. This request aligns the funding with the program costs.

The mission of the California Cadet Corps is to provide California schools and students with a quality educational and leadership development program that prepares students for success in college and the work force. The funding and positions retained for the Corps expansion will fund two positions to expand the Corps by 1,000 cadets (currently there are 4,400).

Staff Recommendation: Approve the May Finance letter, as modified by the CMD's subsequent request related to the Cadet Corps expansion. With regard to the resources for the Cadet Corps, staff recommends approval on a two-year limited-term basis with placeholder supplemental report language requiring the CMD to report annually on expenditures and outcomes.

Vote:

8955 CALIFORNIA DEPARTMENT OF VETERANS AFFAIRS

Department Overview. The California Department of Veterans Affairs (CDVA) promotes and delivers benefits to California veterans and their families. More specifically, the CDVA provides: (1) California veterans and their families with aid and assistance in presenting their claims for veterans' benefits under the laws of the United States; (2) California veterans with beneficial opportunities through direct low-cost loans to acquire farms and homes; and (3) the state's aged and disabled veterans with rehabilitative, residential, and medical care and services in a home-like environment at the Veterans Homes of California (VHCs). The CDVA operates VHCs in Yountville (Napa County), Barstow (San Bernardino County), Chula Vista (San Diego County), and Greater Los Angeles Ventura County (with homes in West Los Angeles, Ventura, and Lancaster).

Budget Overview. The January Governor's Budget proposes to continue to ramp-up admissions at the VHCs in West Los Angeles, Lancaster, and Ventura. The Governor also proposes to provide continued resources and staffing related to the construction and activation of two new VHCs, in Redding and Fresno, both of which are scheduled to begin admissions in early calendar year 2012. The January Governor's Budget provides CDVA with 2,396.5 authorized positions and $399.3 million ($253.4 million GF).

The construction cost of the VHCs was/is funded with $50 million in general obligation bonds available through Proposition 16 (2000), an estimated $212 million in lease-revenue bonds [most recently amended by Chapter 824, Statutes of 2004 (AB 1077)], and federal funds.

Issue Proposed for Discussion / Vote

Issue 1 – Program 30: Veterans Homes of California, Greater Los Angeles Ventura County

Background. The CDVA provides residential and medical care services to honorably discharged California veterans who served on active duty and are over the age of 62 or disabled. The VHCs are long-term residential care facilities that provide California's qualified aged or disabled veterans with rehabilitative, residential, medical, and support services in a home-like environment. Once an eligible veteran selects a VHC as his or her long-term care option, and is approved for admission, the veteran becomes a fee paying resident of the VHC. Spouses of veterans may also be eligible for VHC membership. The VHCs provide a long-term continuum of care, from domiciliary care at one end of the spectrum, which is similar to independent living accommodations, to skilled nursing care at the other end of the spectrum, which provides continuous skilled nursing or rehabilitation services.

March 2011 Budget Package. As part of the March 2011 Budget package, the following resources were approved for the VHCs in 2011-12:

- Net GF increase of $31.7 million for all of the VHCs, including: (1) an augmentation of $24 million for full-year and one-time adjustments to phase-in staffing and residents in the existing and new VHCs in Greater Los Angeles Ventura County (GLAVC), Redding, and Fresno; (2) $4.7 million for furlough and personal leave program reductions which are only reflected in the 2010-11 fiscal year budget; and (3) $9.3 million in increased lease-revenue bond payments for VHC-GLAVC. The expenditures are offset by an increase of $5.0 million in GF revenue.

This funding level is $8.1 million below the Governor's January budget, reflective of savings resulting from: (1) a three-month delay in the opening of the Redding and Fresno VHCs; and (2) the staggered opening of the Residential Care for the Elderly (RCFE) and Skilled Nursing Facility (SNF) levels of care at the Redding and Fresno VHCs. The opening of the Redding home will be delayed from February 2012 to May 2012; the opening of the Fresno home will be delayed from April 2012 to July 2012. In both homes, SNF residents will be admitted in January 2013. The total savings from these combined actions is $8.9 million GF; however, the reduction of offsetting revenue (federal per diem subsidies and resident fees) of $800,000 reduces the overall savings to the $8.1 million GF figure noted above.

Staff Comment. When the Subcommittee acted on Program 30 earlier this year it stated intent to reopen the VHC budget in Spring 2011 when caseloads were known to make any necessary adjustments to the 2011-12 budget to account for salary savings because not all of the positions contained in the request would be hired per the schedule. Given the action to delay the opening of the Redding and Fresno VHCs, the question before the Subcommittee is whether there is any salary savings within the GLAVC VHC request.

The chart below illustrates the resident census at the GLAVC facilities at two points in 2010-11 as compared to the census goal for 2010-11:

VHC	January 17, 2011 Census	May 17, 2011 Census	2010-11 Census Goal
West Los Angeles	21	40	39
Lancaster	22	41	54
Ventura	39	52	54

While the above chart illustrates that the Ventura and West Los Angeles VHCs are on track to reach their 2010-11 census goal, in the case of the Ventura facility that goal was originally estimated to be met in September 2010. In the case of the Lancaster VHC, while significant progress has been made since January to increase resident admissions, that facility is unlikely to reach its target, a target that was originally estimated to be reached in August of 2010.

Given these factors, it is quite likely that there is salary savings in the 2010-11 budget due to the pace of admissions at the GLAVC facilities and the admission level at VHC-Lancaster. Any GF savings in the current year will revert at the end of year automatically, but staff notes that adjustments should potentially be made to the 2011-12 GLAVC budget to account for salary savings, if identified. The LAO is working with the DOF and CDVA, but given time constraints of the May Revision, the final analysis was not complete at the time this agenda was written.

The LAO will present information to the Subcommittee at today's hearing as to its findings.

Staff Recommendation: To the degree salary savings (GF) are identified within the 2011-12 budget for the GLAVC VHC, staff recommends adoption of the LAO's findings.

Vote:

9620 CASH MANAGEMENT AND BUDGETARY LOANS

For additional background on Cash Management and Budgetary Loans, please see the write-up in the vote-only section of the agenda.

Issue Proposed for Discussion / Vote

Issue 1 – Accelerate Repayment of Special Fund Loans

Governor's Proposal: In the May Revision, the Administration proposes to accelerate repayment of $744 million in special fund loans from 2012-13 into 2011-12. Since these loans are repaid from the General Fund, this proposal is a "negative" budget solution, or a budget hit to 2011-12. However, the Governor proposes this action to begin paying off budgetary borrowing that he pegs at $34.7 billion. Among the largest categories of budgetary borrowing are deferrals to K-12 schools and community colleges ($10.4 billion), outstanding Economic Recovery Bonds ($7.1 billion) and loans from special funds ($5.1 billion). So the May Revision proposal would reduce outstanding special fund loans from $5.1 billion to $4.4 billion. The specific loan repayments are listed below.

Loans to be Repaid in 2011-12 (were due in 2012-13)
2011-12 May Revision
(Dollars in Thousands)

Org	Dept	Fund Title	Fund	Amounts
0502	OSCIO	State Emergency Telephone Number Acct	0022	$28,000
1111	DCA	Enhanced Fleet Modernization subaccount	3122	40,000
1110	DCA	Accountancy Board	0704	173
3360	CEC	Renewable Resources Trust Fund	0382	18,200
3360	CEC	Renewable Resources Trust Fund	0382	10,900
3360	CEC	Renewable Resources Trust Fund	0382	35,000
3360	CEC	Alternative and Renewable Fuel and Vehicle Technology Fund	3117	8,250
3360	CEC	Alternative and Renewable Fuel and Vehicle Technology Fund	3117	16,300
3500	DRRR	Beverage Container Recycling Fund	0133	72,277
3500	DRRR	Beverage Container Recycling Fund	0133	99,400
3500	DRRR	Electronic Waste Recovery & Recycling	3065	80,000
3560	SLC	School Land Bank Fund	0347	59,000
3680	DBW	Harbors and Watercraft Revolving Fund	0516	29,000
3790	Parks	Off-Highway Vehicle Trust Fund	0263	90,000
4140	OSHPD	Hospital Building Fund	0121	20,000
4140	OSHPD	Health Data and Planning Fund	0143	12,000
8120	POST	Peace Officers' Training Fund	0268	5,000
8660	PUC	High-Cost Fund-B Administrative Committee Fund	0470	44,000
8660	PUC	High-Cost Fund-B Administrative Committee Fund	0470	15,000
8660	PUC	Teleconnect Fund	0493	61,800
		Total		**$744,300**

Staff Recommendation: Approve the Governor's proposal to start paying down budgetary borrowing.

Vote:

REDUCING STATE GOVERNMENT

Background. The March 2011 budget package recognized $250 million GF ($163 million other funds) for savings associated with the identification of efficiencies in state operations, including identification of agencies, departments, and programs that can be reorganized to eliminate duplication and unnecessary functions; review of state peace officer and safety classifications; and reductions in other areas like contracting, fleet operations, and cell phone use. The mechanism to achieve these savings is a budget control section that provides the Administration with the authority to make the required budgetary reductions to achieve the total savings.

Working from these totals, the Administration has since identified, and in some cases already achieved, savings through a variety of executive actions, including eliminating the offices of the Secretary of Education and the American Recovery and Reinvestment Act Inspector General, banning non-essential travel, implementing a statewide building rental rate reduction, reducing the number of state-issued cellular phones, and reducing the statewide vehicle fleet, including the elimination of any non-essential vehicles and reducing the number of home-storage permits.

The May Revision builds on these executive actions and proposes to specifically reduce state operations by $82.7 million ($41.5 million GF) via the same control section mechanism included in the March 2011 budget package. These savings would be achieved through a variety of eliminations, consolidations, reductions, and efficiencies, including: (1) the elimination of 32 boards, commissions, task forces, and offices; (2) the consolidation of the State Personnel Board and the Department of Personnel Administration; (3) several changes due to realignment, including the elimination of the Departments of Mental Health and Alcohol and Drug Programs and a 25 percent state operations reduction for realigned public safety programs; and (4) various program reductions and efficiencies. The May Revision proposal also includes a comprehensive state asset review to result in the eventual disposition of non-essential or under-utilized state properties; however, any savings from this effort would be included in the 2012-13 budget.

All of the proposed eliminations and consolidations, to the degree that they require statutory changes, cannot be adopted on an urgency basis. Article 4, Section 8 (d), of the California State Constitution states that, “an urgency statute may not create or abolish any office or change the salary, term, or duties of any office, or grant any franchise or special privilege, or create any vested right or interest.” Therefore, the eliminations and consolidations all have an effective date of January 2, 2012, with the associated savings of six months.

Control Sections 3.91 and 13.25, entitled “Reductions in State Operations” and “Reorganizations and Consolidations,” respectively, are in the purview of this Subcommittee and discussed further below. In addition, also discussed below are the specific “Reducing State Government” proposals that fall within the jurisdiction of this Subcommittee. The remaining items are being addressed by the relevant Senate Budget Subcommittee with jurisdiction.

Issues Proposed for Discussion / Vote

Issue 1 – CS 3.91 Reductions in State Operations and CS 13.25 Reorganizations and Consolidations

Governor's Request. In a May Revision Finance letter, the Governor requests revisions to CS 3.91, pertaining to reductions in state operations, which was approved as part of the March 2011 Budget package. These revisions provide additional specificity regarding departmental consolidations, operational efficiencies, and other cost reduction measures.

In addition, and in a separate May Revision Finance letter, the Governor requests that a new control section be added to the 2011-12 budget, CS 13.25 entitled Reorganizations and Consolidations to reflect reorganizations and consolidations of departments or functions of departments that are approved by the Legislature.

Background. The Budget Act is divided into sections. Section 1.00 establishes a citation for the legislation. Section 1.50 provides a description of the format of the act. Section 2.00 contains the itemized appropriations. Sections 4.00 through 99.50 are general sections, also referred to as control sections, which generally provide additional authorizations or place additional restrictions on one or more of the itemized appropriations contained in Section 2.00.

CS 3.91, as approved as part of the March 2011 budget package, requires DOF to reduce each item of appropriation, with the exception of those items for the California State University, Hastings College of the Law, the Legislature, the University of California, and the Judicial Branch, in the total amount of $250 million GF ($163 million other funds) for savings achieved through departmental consolidations, operational efficiencies, and other cost reduction measures, such as reducing contracts.

The May Revision proposal would revise CS 3.91 to identify specific savings of $25.1 million GF ($11.0 million other funds) attributed to a list of departmental consolidations or eliminations identified in the "Reducing State Government" chapter of the May Revision document. The May Revision identifies an additional $16.4 million GF ($30.2 million other funds) from other operational efficiencies. The remaining savings, $208.5 million GF ($121.8 million other funds), would be achieved as proposed in the March 2011 budget package.

CS 13.25 is intended to serve as the mechanism for DOF to adjust budgets upwards, should the Legislature approve certain consolidations or other reductions that require such an action. For instance, should the Legislature approve the elimination of the Fair Employment and Housing Commission (discussed as Issue 2 below), certain functions and responsibilities would be moved to the Department of Fair Employment and Housing and that department's budget would need to be adjusted upwards.

Staff Comment. These control sections are the most effective budgetary process available at present to accomplish this task of reducing state government. Through the control sections, the DOF is given the authority to make necessary budget adjustments consistent with legislative approval. However, it is important to strike an appropriate balance and to ensure that, if the Legislature rejects some of the proposals to reduce state government, those proposals are not then adopted through the control section mechanism. In addition, the current wording of CS 13.25 is not clear as to the Administration's intent (to adjust certain budget items upwards). All of these issues can be addressed going forward; staff, therefore, recommends that the Subcommittee approve these control sections on a placeholder basis, pending further language refinements and to accommodate the work of the other budget Subcommittees who are considering reduction proposals in hearings that either occurred yesterday, are happening today or are happening tomorrow. In addition, staff recommends that the Subcommittee approve Supplemental Report Language to provide greater clarity as to legislative intent and action on the May Revision "Reducing State Government" proposals.

Staff Recommendation: Approve Control Sections 3.91 and 13.25 on a placeholder basis, along with placeholder Supplemental Report Language, pending further language refinements and to incorporate the actions of the other budget subcommittees on the May Revision proposals.

Vote:

Issue 2 – Secretary for State and Consumer Services (0510) GF Budget Reduction and Elimination of Offices of the Insurance Advisor and Privacy Protection

Agency Overview. The State and Consumer Services Agency (SCSA) oversees the departments of Consumer Affairs, Fair Employment and Housing, and General Services. The Agency also oversees the California Science Center, the California African American Museum, the Seismic Safety Commission, the Fair Employment and Housing Commission, the Franchise Tax Board, the California Building Standards Commission, the State Personnel Board, the California Public Employees' Retirement System, the California State Teachers' Retirement System, the Victim Compensation and Government Claims Board, the Office of Privacy Protection, and the Office of the Insurance Advisor.

The entities under the SCSA are responsible for civil rights enforcement, consumer protection, and the licensing of 2.5 million Californians in more than 240 different professions. Agency entities provide oversight and guidance for the procurement of more than $8.9 billion worth of goods and services; the management and development of state real estate; operation oversight of two state employee pension funds; collection of state taxes; hiring of state employees; adoption of state building standards; and the administration of two state museums. In addition, the Secretary for State and Consumer Services Agency is the Chair of the California Building Standards Commission and the Victim Compensation and Government Claims Board, and operates the Office of Privacy Protection.

Budget Overview. The Governor's May Revise Budget provides 10.1 authorized positions and $1.75 million ($202,000 GF). This is a decrease of $789,000 GF, $250,000 in reimbursements, and 5.2 positions from the January Budget.

Proposal 1: Eliminate General Fund for the Agency

Governor's Request. As part of the May Revision, the Governor requests a decrease of $965,000 all funds ($548,000 GF) in 2011-12. This would eliminate GF support for SCSA and require departments under the SCSA's purview to reimburse the SCSA for operational expenses. This decrease will be offset by an increase of $965,000 from reimbursements in 2011-12.

Background. Reimbursement-based funding is already used by the California Labor and Workforce Development Agency. This model of funding operations is based on the establishment of inter-agency agreements between the Agency and the departments it oversees. DOF has stated that the department budgets would not be increased to accommodate increased expenditures from supporting SCASA operations.

Staff Recommendation: Approve the May Revision request.

Vote:

Proposal 2: Eliminate Office of Insurance Advisor

Governor's Request. As part of the May Revision, the Governor requests a decrease of $250,000 (reimbursements) and 1.9 personnel years in 2011-12 from the elimination of the Office of Insurance Advisor (OIA).

Background. Following the removal of the Department of Insurance from the administration and the creation of an elected Insurance Commissioner pursuant to Proposition 103, the OIA was established in 1991 in order to provide the Governor's Office with independent policy advice on insurance matters makes policy recommendations on legislation. The OIA tracks, monitors, analyzes and makes policy recommendations on pending legislation affecting various lines of insurance coverage, including: annuities, automobile, bonds, commercial, disability, earthquake, flood, health, homeowners, life, long-term care, and workers' compensation.

Staff Recommendation: Approve the May Revision request.

Vote:

Proposal 3: Eliminate Office of Privacy Protection

Governor's Request. As part of the May Revision, the Governor requests a decrease of $435,000 all funds ($250,000 General Fund), as well as 3.3 positions in 2011-12, through the elimination of the Office of Privacy Protection (OPP). This would provide half-year funding for OPP, which would allow it to be phased out. The total 2010-11 budget for OPP is $701,000 and seven positions.

Background. The OPP is established in statute to "protect the privacy of individuals' personal information in a manner consistent with the California Constitution by identifying consumer problems in the privacy area and facilitating the development of fair information practices…". The OPP's mission is to be a resource and advocate on privacy issues. In addition to providing information and education for consumers, the OPP also makes privacy practice recommendations to businesses and other organizations. OPP's primary activities include:

- Providing information and assistance to individuals on identity theft and other privacy concerns;
- Educating consumers, businesses, and other organizations on privacy rights and practices;
- Coordination with law enforcement on identity theft, data breach, and other topics; and
- Providing recommendations to organization of privacy policies and practices that promote and protect the interests of California consumers.

Staff Comment. OPP has unique tasks in assisting consumers in understanding and addressing identify theft. Also, OPP is very effective in providing assistance to the Legislature in understanding challenges facing consumers and law enforcement.

Staff Recommendation: Reject the May Revision request and refer the matter to policy committee.

Vote:

Issue 3 – Secretary for Business, Transportation, and Housing (0520) Decrease State Matching Funds for Tourism Office

Governor's Request. As part of the May Revision, the Governor requests a decrease of $734,000 GF in 2011-12 for the Tourism Office.

Background. The California Office of Tourism works closely with the California Travel and Tourism Commission (CTTC) (a 501 c (6) non-profit organization) with the mission to develop and maintain marketing programs, in partnership with the state's travel industry, to promote the State of California as a premier travel destination.

The CTTC is funded primarily through assessments to businesses in the travel and tourism industry (Accommodations, Restaurant and Retail, Attractions, Transportation and Travel Industry, Passenger Car Rental Industry). These assessments are self-imposed and are renewed every six years, with the next renewal coming in 2013. In addition to the assessment fees, the CTTC also receives a total of $934,000 from the State General Fund to fund some of the Commission's marketing activities.

Staff Comment: The May Revision proposal would reduce General Fund support from $934,000 to $200,000 – enough to maintain the public-private partnership and support the Executive Director. The tourism industry would continue to support the marketing of California tourism through $50 million in industry self-assessed fees.

Staff Recommendation: Approve May Revision request.

Vote:

Issue 4 – Fair Employment and Housing Commission (1705) Eliminate the Fair Employment and Housing Commission

Governor's Request. As part of the May Revision, the Governor requests to eliminate the Fair Employment and Housing Commission (FEHC), with adjudication of employment and housing discrimination cases instead appealed to the Director of the Department of Fair Employment and Housing (DFEH) beginning January 1, 2012, effectively consolidating workload for savings of $438,000 ($344,000 GF) and 1.4 personnel years in 2011-12. This request includes proposed budget trailer bill language.

Background. The FEHC is a quasi-judicial administrative agency which enforces state civil rights laws regarding discrimination in employment, housing, and public accommodations; pregnancy disability leave; family and medical leave; and hate violence. The FEHC is comprised of seven members, appointed by the Governor and confirmed by the Senate. Members receive $100/day per diem. In 2010-11, the FEHC was budgeted at $1.2 million ($1.034 million GF) and 5.2 authorized positions. The chart below displays the 2010 FEHC case adjudication statistics:

2010 FEHC Case Adjudication Statistics

Accusations Filed by DFEH	59
Hearings calendared by FEHC for three day evidentiary hearings	55
Evidentiary hearings (number of hearings/number of hearing days)	14/29
Case Management Conferences	29
Early Mediation Evaluation Conferences	39
Settlement Conferences/Mediations with Commissioners & staff	6

As part of its proposal to eliminate the FEHC, the Administration indicates that it will consult with stakeholders and evaluate options to phase out the stand-alone FEHC that handles these cases by January 1, 2012. Under the "phase out" plan, the DFEH will employ administrative law judges and, instead of the Commission deciding cases, DFEH's Director (or his/her designee) will decide the case. Rules to interpret the Fair Employment and Housing Act will be issued by DFEH following the current public rule-making process.

Staff Comment. In considering this request, staff notes that a key issue is the adjudicative process and the retention of an entity that can effectively enforce the state's civil rights laws. More specifically, the transition must be done in a precise way to ensure that the FEHC's adjudicatory and regulatory responsibilities are transferred properly, taking into consideration potential conflicts between prosecuting cases (currently through the DFEH) and adjudicating these cases (currently through the FEHC). This request is also accompanied by lengthy budget trailer bill language. As such, and in considering this request, the Subcommittee may wish to refer this proposal to the Senate Judiciary and Transportation and Housing Committees for further review of its impacts as well as potential new approaches.

Staff Recommendation: Reject the May Revision request and and refer the matter to policy committee.

Vote:

Issue 5 – Department of Housing and Community Development (2240) Various Budget Reductions

Governor's Request. As part of the May Revision, the Governor requests to reduce the Department of Housing and Community Development's GF budget by a total of $1.168 million and 9.9 positions, as detailed in the below chart. These requests do not include any proposed budget trailer bill language.

	Description	Proposed Reduction	Fund Source
1	Eliminate Housing Policy Funding, within Division of Housing Policy Development	$1.3 million and 8.5 positions	GF
2	Eliminate Preservation Technical Assistance	$35,000	GF
3	Eliminate Redevelopment Housing Funds Oversight	$123,000 and 1.4 positions	GF
4	Eliminate Child Care Monitoring Support	$10,000	GF

General Department and Budget Background. A primary objective of the Department of Housing and Community Development (HCD) is to expand housing opportunities for all Californians. The HCD administers housing finance, economic development, and rehabilitation programs with emphasis on meeting the shelter needs of low-income persons and families, and other special needs groups. HCD also administers and implements building codes, manages mobilehome registration and titling, and enforces construction standards for mobilehomes. The January Governor's Budget provides the HCD 598.6 authorized positions and $256.0 million ($8.8 million GF). This is a decrease of 6.5 positions and $490.0 million (the majority of the HCD's expenditures are supported by general obligation bond revenue). Therefore, HCD's budget has been steadily decreasing in recent years due to the pending exhaustion of housing bond funds.

Proposal 1: Eliminate Housing Policy Funding

Background. This proposal would eliminate $1.3 million GF and 8.5 positions that support housing policy in the HCD Division of Housing Policy Development (HPD). HPD identifies California's housing needs and develops policies to meet those needs. HPD administers state housing element law, including the review of local general plan housing elements. HCD reports that administering the state's housing element law is the biggest workload driver in HPD. This reduction would decrease HPD's 2011-12 staffing level from 12.5 to 3.5 positions. With that reduced level of staff, HPD would be unable to meet its current workload and would have to ratchet down workload to meet the limited resources available.

The remaining 3.5 positions would be funded as follows: (1) $98,000 from the Air Pollution Control Fund; (2) $1.068 million from the Housing Related Parks program – this resource actually funds a total of seven positions, two of which are assigned to housing element workload; and (3) $136,000 from reimbursements funding from the HCD Division of Financial Assistance (DFA) in recognition of support to DFA programs by HPD.

Staff Comment. HCD review of housing elements has proven critical to ensuring cities and counties create opportunities (zoned land, funding, etc.) for affordable housing. Without that effort on the part of HCD, it does not appear there is another viable method to ensure compliance with housing element law. As such, the LAO is currently providing technical assistance to staff to determine the viability of alternative funding sources to support HPD's housing element-related workload. Three potential fund sources are: (1) Proposition 84; (2) Housing-Related Parks Bond (Propositions 1C and 46); and/or, (3) Proposition 46 Building Equity and Growth in Neighborhoods (BEGIN). As noted above, HRP funds currently provide support for two of the HPD's positions.

Staff Recommendation. Approve the May Revision request contingent on the identification of an alternative fund source to support housing element workload in the Housing Policy Division.

Vote:

<u>Proposal 2: Eliminate Preservation Technical Assistance</u>

Background. This proposal would eliminate $35,000 GF utilized to provide assistance in the prevention of subsidized housing converting to market rents upon the expiration of the subsidy period. On an annual basis, HCD has awarded a contract totaling $65,000 ($35,000 GF and $30,000 other funds) for this work.

HCD estimates that 78,503 affordable homes are determined to be at-risk of conversion by private owners over the next five years. Because it generally costs half as much and takes half the time to maintain existing affordable housing than building it new, HCD contracts with the California Housing Partnership Corp. (CHPC) to provide technical assistance on preservation issues both with project sponsors as well as to provide technical assistance to persons in preparing local housing elements that are required to include inventories of, and programs for preserving, at-risk properties. These inventories identify at-risk projects with expiring Section 8 contracts and/or federal, state or local subsidized or below market mortgages eligible for prepayment within five years of the term expiration.

HCD indicates that the CHPC investigates the status of potentially at-risk projects by utilizing specific project information from its database, contacts property owners to determine their intentions, and uses its statewide network to identify a preservation purchaser.

Staff Comment. Notwithstanding the merits of providing preservation technical assistance, it is not clear to staff why this should be a state GF cost. It is also not clear why the GF costs could not be supported by federal funds, since a great number of the state's affordable housing units are federally-subsidized and in the Section 8 program. Therefore, staff recommends the Subcommittee approve this request.

Staff Recommendation. Approve the May Revision request.

Vote:

Proposal 3: Eliminate Redevelopment Housing Funds Oversight

Background. This proposal would eliminate $123,000 GF and 1.4 positions that support HCD oversight of redevelopment agency (RDA) low- and moderate-income housing funds and an annual report on housing funds and activities.

Staff Comment. Staff notes that the primary function here is the compiling of a report of the reports submitted by RDAs. The Administration indicates that this proposal is consistent with the broader proposal to eliminate RDAs. Staff also notes that under current law RDAs are required to submit annual financial transaction and compensation reports to the State Controller's Office.

Staff Recommendation. Approve the May Revision request.

Vote:

Proposal 4: Eliminate Child Care Monitoring Support

Background. This proposal would eliminate $10,000 GF for child care monitoring support. Prior to 2004-05, HCD administered two GF-funded funds that were intended to provide loans and loan guarantees for private child care centers. In 2004-05, the Budget Act transferred the remaining money from those funds back to the GF, but the funds themselves were not abolished. In 2009, the funds were abolished as part of the general government budget trailer bill. HCD is proposing a state operations reduction of $10,000 GF.

Staff Comment. While it is correct that the state has not made any new awards under this program in many years, the prior awards required a commitment for the child care provider to provide care for an extended period of time. HCD indicates that there are still 14 child care loans outstanding that HCD must administer. The last of these loans have a payoff in 2033. Staff notes that $10,000 in funding would provide support for roughly 0.1 percent of one position. As such, this workload would appear to be absorbable within existing resources.

Staff Recommendation: Approve the May Revision request.

Vote:

Issue 6 – Commission on the Status of Women (8820) Elimination of the Commission on the Status of Women

Department Overview. The Commission on the Status of Women (CSW) is an independent, non-partisan agency working to advance the causes of women. Toward that end, the CSW influences public policy by advising the Governor and the Legislature on issues impacting women and educating and informing its constituencies-thereby providing opportunities that empower women and girls to make their maximum contribution to society. The CSW consists of a 17-member body including the Superintendent of Public Instruction, the Labor Commissioner, three Assembly members and three Senators. Nine of the 17 members are public members: one appointed by the Speaker of the Assembly; one by the Senate Committee on Rules; and seven are appointed by the Governor. Public members serve four-year terms and are reimbursed for necessary expenses.

Budget Overview. The Governor's January Budget provided the CSW with $467,000 total funds ($464,000 GF and $2,000 reimbursements) and 4.3 positions.

Governor's Request. As part of the May Revision, the Governor requests a decrease of $234,000 all funds ($233,000 GF) and 2.1 personnel years in 2011-12 in order to eliminate the CSW.

Background. The Governor's justification for the elimination of the CSW is that there are numerous formal and informal avenues for the Governor and Legislature to seek advice on public policy issues impacting women. However, the CSW has many unique tasks. The CSW is the only state agency that looks specifically at all issues impacting women. The CSW holds public hearings across the state to gather input on issues important to women, and uses that information to develop a public policy agenda. Also, the CSW provides the Legislature, Governor, and advocates with gender analysis on proposed bills and actions. On its website, CSW provides a wide variety of information and resources on issues impacting women and girls. Also, CSW facilitates the development of coalitions of diverse organizations around various issues such as reproductive rights, paid family leave, incarcerated women, etc.

Staff Recommendation: Reject the May Revision request and refer the matter to policy committee.

Vote:

Issue 7 – Department of Finance (8860) Accelerate the End of the California Recovery Task Force

Governor's Request. As part of the May Revision, the Governor requests to eliminate the California Recovery Task Force by January 1, 2012, for savings of $0.8 ($0.4 million GF and $0.4 million Central Service Cost Recovery Fund) and 3.4 positions. This request does not include any proposed budget trailer bill language.

Background. On February 17, 2009, President Obama signed the American Recovery and Reinvestment Act (ARRA), a $787 billion federally-funded economic stimulus plan for a wide range of federal, state, and local programs as well as tax relief for qualified businesses and individuals. ARRA also created new requirements for state-level oversight and reporting of stimulus dollars provided to state entities. Both the 2009-10 and 2010-11 budgets provided funding for California's ARRA accountability framework, comprised of four organizational components: the California Recovery Task Force (CRTF); the ARRA Inspector General (ARRA IG); the Bureau of State Audits (BSA); and, the State Controller's Office (SCO). Both the BSA and SCO were pre-existing entities, while the CRTF and ARRA IG were established via Executive Order by the Governor in Spring 2009. In January 2011, Governor Brown announced he was eliminating the ARRA IG's Office six months early (funding for that office in the 2010-11 budget was provided on a one-year limited-term basis). Any outstanding audit activities of that office were transferred to the SCO or BSA.

Building on a legislative action in the March 2011 budget package, which reduced the California Recovery Task Force by $393,000 ($224,000 GF and $169,000 Central Service Cost Recovery Fund), the May Revision proposes to eliminate the Task Force on January 1, 2012, for additional savings of $800,000 ($400,000 GF) and 3.4 positions. Under the May Revision proposal, any remaining federally-mandated quarterly reporting will be decentralized to the appropriate state department.

Staff Recommendation: Approve the May Revision request.

Vote:

Senate Budget and Fiscal Review—Mark Leno, Chair

SUBCOMMITTEE NO. 4 Agenda

Senator Michael J. Rubio, Chair
Senator Noreen Evans
Senator Doug LaMalfa

Thursday, May 26, 2011
10:00 a.m.
Room 112

Consultants: Brian Annis, Kris Kuzmich, and Seija Virtanen

AGENDA PART B

OUTCOMES

DEPARTMENTS TO BE HEARD

(Please See Detailed Agenda on Pages 2 and 3 for More Specific Listing and Order of Departments and Issues to Be Heard)

0510	Secretary for State and Consumer Services
0520	Secretary for Business, Transportation, and Housing
0840	State Controller
0845	Department of Insurance
0911	Citizens Redistricting Commission
0950	State Treasurer
1705	Fair Employment and Housing Commission
1730	Franchise Tax Board
1760	Department of General Services
2240	Department of Housing and Community Development
2400	Department of Managed Health Care
8820	Commission on the Status of Women
8860	Department of Finance
8885	State Mandates
8940	Military Department
8955	California Department of Veterans Affairs
9600	Debt Service General Obligation Bonds & Commercial Paper
9620	Cash Management and Budgetary Loans
9860	Capital Outlay Planning and Studies Funding
CS 3.91	Reductions in State Operations
CS 4.30	Lease Revenue Payment Adjustments
CS 13.25	Reorganizations and Consolidations

AGENDA – VOTE ONLY ITEMS

(Please see summary chart on Pages 4 and 5)

AGENDA – DISCUSSION / VOTE ITEMS

Issues Proposed for Vote Only:

	Issue	Amount	Fund Source	Staff Recommendation
	Treasurer's Office (0950)			
1	Budget Bill Language for Bond Issuance Costs	$0 and BBL	Not applicable	APPROVE
	Department of General Services (1760)			
1	California Institute for Women Walker Clinic and Infirmary Buildings Structural Retrofit Project Reappropriation	$5,951,000	Seismic Bonds	APPROVE
2	Office Building 10 Renovation Project Extension	$437,000	Lease-Revenue Bonds	APPROVE
3	California Department of Transportation District 3 Office Replacement Project Extension	$851,000	Lease-Revenue Bonds	APPROVE
4	Provisional Language, California Health Care Facility Construction Services	N/A	N/A	APPROVE, as specified
	Department of Housing and Community Development (2240)			
1	Community Development Block Grant Service Funding Adjustment	$1,100,000 shift to local assistance and (-) 10 positions	Federal Funds	APPROVE
2	Propositions 46 and 1C Liquidation Extension Building Equity and Growth in Neighborhoods	N/A	N/A	APPROVE
3	Liquidation Extension *Vega et al. v. Richard Mallory* Settlement	N/A	N/A	APPROVE
4	Federal Neighborhood Stabilization Program Round 3	$11,300,000	Federal Funds	APPROVE
	Department of Managed Health Care (2400)			
1	Federal Grant Funds	$3,900,000	Federal Funds	APPROVE
	Commission on State Mandates (8885)			
1	Conforming Changes for State Local Realignment	$0 and BBL	N/A	APPROVE
2	Savings Based on State Controller's April 30 Report	-$3,900,000 (savings)	GF	APPROVE
	Debt Service General Obligation Bonds & Commercial Paper (9600)			
1	May Revision: New Estimates of Bond Debt Service	-$267,000,000 (savings)	GF	APPROVE
	Cash Management and Budgetary Loans (9620)			
1	Intra-year Payment Deferrals / Cashflow Loans	-$50,000,000 (savings)	GF	APPROVE

Issues Proposed for Vote Only, Continued:

	Capital Outlay Planning and Studies Funding (9860)			
1	Unallocated Capital Outlay Budget Reduction	$500,000	GF	APPROVE
	Lease-Revenue Payment Adjustments (CS 4.30)			
1	Various Lease-Revenue Bond Debt Service Adjustments	$471,000 $4,047,000	GF Other Funds	APPROVE

Vote: All vote-only items approved by a 3-0 vote with <u>the exception of Budget Item 2400, Department of Managed Health Care, Federal Grant Funds,</u> which was approved by a vote of 2-1 with Senator LaMalfa voting no.

Issues Proposed for Vote Only – Issue Descriptions

STATE TREASURER (0950)

Department Overview: The State Treasurer's Office (STO), a constitutionally established office, provides banking services for state government with goals to minimize interest and service costs and to maximize yield on investments. The Treasurer is responsible for the custody of all monies and securities belonging to or held in trust by the state; investment of temporarily idle state monies; administration of the sale of state bonds, their redemption and interest payments; and payment of warrants drawn by the State Controller and other state agencies.

January Governor's Budget Overview: The Governor proposed expenditures of $27.4 million ($4.7 million GF) and 229.7 positions – an increase of $981,000 (a GF increase of $43,000) and no change in positions. The year-over-year budget increase is primarily a result of employee compensation adjustments.

March Budget: In the March budget package, the Legislature approved the Treasurer's budget as proposed by the Governor.

Issue 1 – Budget Bill Language for Bond Issuance Costs

Budget Request: In the Governor's May Revision, the Treasurer's Office requests new budget bill language that would allow a GF augmentation of up to $800,000 only if needed due to a cancelled bond sale. If bonds are sold at market, bond proceeds are used to pay advertising expenses and rating agency fees. In rare cases, bond sales have been cancelled after costs are incurred for advertising expenses and rating agency fees. In those cases, there is no timely mechanism for the Treasurer to obtain funding for these costs.

Staff Comment: The Treasurer is not requesting a budget augmentation, but rather language that would allow the Director of Finance to approve an augmentation of up to $800,000 only if necessary due to a cancelled bond sale. Any such approval by the Director of Finance would be followed by notification to the Joint Legislative Budget Committee.

Staff Recommendation: Approve the May Finance letter.

DEPARTMENT OF GENERAL SERVICES (1760)

Department Overview. The Department of General Services (DGS) provides management review and support services to state departments. The DGS is responsible for the planning, acquisition, design, construction, maintenance, and operation of the state's office space and properties. It is also responsible for the procurement of materials, data processing services, communication, transportation, printing, and security.

Budget Overview. The January Governor's Budget provides the DGS with 3,923.8 authorized positions and $1.1 billion ($5.5 million GF). This is a decrease of eight positions and $18.5 million. As a central service agency, the vast majority of DGS' budget is comprised of special fund and reimbursement revenue, received for services performed for other state departments and agencies.

Issue 1 – California Institute for Women Walker Clinic and Infirmary Buildings Structural Retrofit Project Reappropriation

Governor's Request. In an April Finance Letter, the Governor requests to reappropriate a total of $5.951 million (seismic bonds) of working drawing and construction funds for the structural retrofit of the Walker Clinic and Infirmary Buildings at the California Institute for Women, Corona (CIW).

2010-11 Budget. The 2010-11 Budget provided funding in the amount of $5.452 million for the construction phase of the CIW project; total estimated costs are $6.402 million, including $85,000 – study phase, $393,000 – preliminary plans, and $472,000 – working drawings.

Background. The CIW houses all custody levels of female inmates and functions as a reception/processing center for incoming female inmates. In addition to its large general population, CIW houses inmates with special needs such as pregnancy, psychiatric care, methadone, and medical problems. The Walker Clinic and Infirmary Buildings were assessed and found to be seismically deficient, placing inmates, staff, and visitors at risk in the event of an earthquake. This project consists of a "structural only" retrofit, whereby the majority of the work will be accomplished with minimum disruption to existing interior work space functions.

Working drawing funds were originally provided in 2007-08; construction funds were provided in 2010-11. The schedule for this project was delayed due to the Pooled Money Investment Board's December 2008 action freezing all disbursements from AB 55 loans (which in turn caused numerous project suspensions). The CIW project was subsequently reactivated and working drawings are substantially complete; however, some minor work remains outstanding. As a result, it will not be possible for DGS to proceed to bid for construction by June 30, 2011. Therefore, in order to complete the design and eliminate the risk of losing the availability of construction funds, DGS is requesting a one-year reappropriation of funds until June 30, 2012.

Staff Comment. This project has been in the design phase for over four years; DOF indicates that this project will proceed to the construction phase in 2011-12. Further, DOF has verified that there are no intersections between this project and the federal receiver or AB 900 prison construction program.

Staff Recommendation. Approve the April Finance letter.

Issue 2 – Office Building 10 Renovation Project Extension

Governor's Request. In an April Finance Letter, the Governor requests to extend by one year the encumbrance and liquidation period for $437,000 (lease-revenue bonds) in construction funds for the Building Office 10 Renovation project.

2010-11 Budget. The 2010-11 Budget extended by one year, until June 30, 2011, the liquidation period for $569,000 (lease-revenue bonds) for the construction phase of the Office Building 10 Renovation project. It was reported at that time that while the project was substantially complete, some minor work related to the floors in the building remained outstanding, necessitating the one-year extension.

Background. Office Building 10 is located at 721 Capitol Mall. Built in the 1950s, it is one of the oldest buildings located on this part of Capitol Mall. It is a six-story, 148,000 gross square foot building that was renovated from January 2006 through October 2007 and was accepted in December 2007. Prior to its renovation, Office Building 10 was occupied by the Department of Education for 31 years; the Department of Rehabilitation has occupied the building since October 2007. The 2010-11 extension allowed completion of post-construction work to correct first floor junction boxes and the surrounding flooring. The current extension request will accommodate completion of a number of accessibility and security items identified after occupancy, primarily related to the installation of security card readers for strategic points within the building. This work cannot be completed prior to expiration of the current liquidation period of June 30, 2011. Therefore, DGS requests a one-year extension of the liquidation period to complete the project.

Staff Comment. The Office Building 10 Renovation project is now three and half years from acceptance. In 2010-11, the liquidation period was extended by one year to allow for floor repairs. DGS is requesting an additional one year extension in 2011-12. Given that this project was accepted nearly three and a half years ago, a question can be raised about how the needed work could still be considered "post construction warranty work." The fund source is lease revenue bonds, and the use of those funds is for either the Office Building 10 project or debt service related to the project. DOF has indicated that it is more cost effective and efficient to use the existing construction contract for one more year to finish this work; letting a new contract would add time to the schedule to get the needed repairs done. Further, the tenant in the building is the Department of Rehabilitation, so the accessibility issues need to be resolved. Approximately $200,000 of the $437,000 available will be used for this work in 2011-12; the remaining funds will then go to debt service.

Staff Recommendation. Approve the April Finance letter.

Issue 3 – California Department of Transportation District 3 Office Replacement Project Extension

Governor's Request. In an April Finance Letter, the Governor requests to extend by one year the encumbrance and liquidation period for $851,000 (lease-revenue bonds) in construction funds for the California Department of Transportation District 3 Office, Marysville, Office Replacement project.

Background. Funds were originally provided in 2003-04, reappropriated in 2005-06 with an additional supplemental appropriation that year. These funds must be liquidated by June 30, 2011, or the authority will revert. Although construction is currently nearing completion, the project suffered a schedule delay due to the Pooled Money Investment Board's December 2008 action freezing all disbursements from AB 55 loans. As a result of this delay, DGS extended the construction completion date to April 15, 2011. However, DGS is still seeking Leadership in Energy & Environmental Design (LEED) certification and requires additional time to complete close-out activities related to contract acceptance. As a result, DGS requests a one-year extension of the liquidation period to complete the project.

Staff Recommendation. Approve the April Finance letter.

Issue 4 – Provisional Language, California Health Care Facility Construction Services

Governor's Request. In a May Revision Finance letter, the Governor requests to add provisional budget bill language that authorizes the DOF to augment DGS for additional workload costs related to construction inspection services for the California Health Care Facility (CHCF) project in Stockton.

Background. Funding for the CHCF project is pending approval by the State Public Works Board, thus the timing of the CHCF project is uncertain. Site construction is anticipated to begin in late 2011 or early 2012 and the facility will be staffed and occupied by December 2013. As a result of this uncertainty, the level of resources required to provide mandated inspection services is also unknown. This language will enable the DGS to request funding based on the timing of inspection services after project funding has been secured. It will also provide DOF time to review and approve resources requested and require notification to the Legislature.

Staff Comment. This provisional language is warranted. However, staff notes that the proposed language would allow DGS, with the prior written consent of DOF and based on any augmentation made in accordance with the provision, to potentially increase rates charged to other departments for services or the purchases of goods. Staff notes that no compelling case has been made as to why, under any circumstance, an augmentation under this provision would result in a DGS need to increase other departments' rates. Therefore, in considering this request, staff recommends that the following wording be removed from the proposed language:

1760-001-0602

1. (a) Notwithstanding Provisions 3 and 4 of Item 1760-001-0666, the Director of Finance may augment Item 1760-001-0602, when the State Public Works Board has approved the California Health Care Facility project in Stockton. Any augmentation that is deemed necessary on a permanent basis shall be submitted for review as part of the normal budget development process. Any augmentation made in accordance with this provision shall not result in an increase in any rate charged to other departments for services of the purchase of goods ~~without the prior written consent of the Director of Finance~~.
   (b) Any augmentation made pursuant to Section (a) of this provision shall be reported in writing to the chairpersons of the fiscal committees of each house of the Legislature and the Chairperson of the Joint Legislative Budget Committee within 30 days of the date the augmentation is approved. This notification shall be provided in a format consistent with normal budget change request, including identification of the amount of, and justification for, the augmentation, and the program that has been augmented.

Staff Recommendation. Approve the May Finance letter, as modified.

DEPARTMENT OF HOUSING AND COMMUNITY DEVELOPMENT (2240)

Department Overview. A primary objective of the Department of Housing and Community Development (HCD) is to expand housing opportunities for all Californians. The Department administers housing finance, economic development, and rehabilitation programs with emphasis on meeting the shelter needs of low-income persons and families, and other special needs groups. It also administers and implements building codes, manages mobilehome registration and titling, and enforces construction standards for mobilehomes.

Budget Overview. The January Governor's Budget provides the HCD 598.6 authorized positions and $256.0 million ($8.8 million GF). This is a decrease of 6.5 positions and $490.0 million. The majority of the HCD's expenditures are supported by general obligation bond revenue; the HCD's budget has been steadily decreasing in recent years due to the pending exhaustion of housing bond funds.

Issue 1 – Community Development Block Grant Service Funding Adjustment

Governor's Request. As part of the January budget, the Governor requests a shift of $1.1 million in federal budget authority from State Operations to Local Assistance and a reduction of ten positions for the Community Development Block Grant (CDBG) program to reflect a correction in federally allowable administrative costs. To accommodate the reduced level of program administration funding, HCD plans to make programmatic changes which are discussed further below.

Prior Subcommittee Action. This request was denied without prejudice at the Subcommittee's January 27, 2011 hearing, to allow time for the impacts of these proposed changes to be fully analyzed and determine if there were other approaches that could be developed that would have less programmatic impact on recipient communities.

Background. HCD's CDBG program was established over twenty-eight years ago to address the fact that California's non-entitlement jurisdictions, which are smaller communities (many of which are rural and economically distressed), lack the resources and/or economies of scale to receive, award, and monitor these federal grants in an efficient and effective manner that allocates the funds to the most pressing needs, meets all federal requirements, and protects against fraud. HCD's CDBG program currently serves 168 non-entitlement jurisdictions.

Although HCD has authority for 28 positions, the federal funding available is only sufficient to support 18 of those positions. The source of the current problem is a combination of short- and long-term factors and some recent issues regarding the funding for the HCD administration of the CDBG program, including: (1) the complexity and scope of the program makes it labor intensive to administer; (2) the federal allowance for state administration costs for the program is minimal; and, (3) the $1.1 million increase in the program budget in 2007-08, which included a shift of $697,000 CDBG program administration funding from GF to federal funds, cannot be sustained due to federal restrictions.

In response to concerns raised at the Subcommittee's January 27, 2011, hearing HCD worked with its CDBG Advisory Committee, comprised of a combination of CDBG jurisdictions, consultants, and non-profit organizations, to develop and finalize a set of new policies to ensure the broadest possible eligibility for local governments and the continued effective operation of this valuable federal resource, as follows:

1. Super NOFA – One combined Notification of Funding Availability (NOFA) to be released annually each January.
2. 50 Percent Rule – Jurisdictions with open contracts must expend 50 percent of their funds before being eligible for additional funding to encourage jurisdictions to spend the funds and increase the State's expenditure rate with federal Housing and Urban Development. This policy would also increase the number of jurisdictions that HCD funds as new jurisdictions will be coming in every other year for funding.
3. Funding Based on Demand – The amount of funds eligible for an activity would be determined by demand or regulatory minimum requirements.
4. Increased Maximums – Increase the maximum funding requests to $2 million (from $1 million) and increase the maximums on the activities. The biggest increase would be for the Public Improvement projects from $800,000 to $1.5 million. In HCD roundtables and committee meetings, it has been a common theme that jurisdictions want the ability to fund public improvement projects and that the current maximum was too low.
5. Limit of Three Activities per Application – A jurisdiction may be awarded one, two, three, or none depending on demand for each activity.

Staff Comment. The budgetary adjustment must be adopted due to federal requirements; the question of how it will be implemented and its impact on recipient communities raised concerns for the Subcommittee when this request was heard earlier this year. The revised implementation policies before the Subcommittee respond to those concerns and should ensure the broadest possible eligibility for the recipient communities.

Staff Recommendation: Approve the budget request.

Issue 2 – Propositions 46 and 1C Liquidation Extension Building Equity and Growth in Neighborhoods

Governor's Request. In a May Revision Finance letter, the Governor requests an extension of the liquidation dates for the three Building Equity and Growth in Neighborhoods (BEGIN) program Budget Act appropriations. The affected budget act appropriations and liquidation dates are for the 2005-06, 2006-07, and 2007-08 fiscal years. For the 2005-06 and 2006-07 appropriations, it is requested that the liquidation period be extended from June 30, 2011, to June 30, 2013. For the 2007-08 appropriations, it is requested that the liquidation period be extended from June 30, 2012 to June 30, 2013.

Background. The BEGIN programs make grants to qualifying cities, counties, or cities and counties to be used for down payment assistance to qualifying first-time home buyers of low and moderate incomes purchasing newly constructed homes in a BEGIN project. In order to qualify, an applicant city, county, or city and county must provide regulatory relief and fee reductions to developers. The Administration is seeking these liquidation extensions because while the applicant jurisdictions have provided the regulatory relief as required by the BEGIN awards, additional time is needed for liquidation to provide the time necessary to fulfill the final steps of the program obligations, complete projects, and find qualified homebuyers.

Staff Comment. While these appropriations were originally made in different years, the requested liquidation extensions are two years and one year, respectively. The Administration indicates this is to reduce administrative program costs by placing these appropriations on the same "cycle."

Staff Recommendation. Approve the May Finance letter.

Issue 3 – Liquidation Extension Vega et al. v. Richard Mallory Settlement

Governor's Request. In a May Revision Finance letter, the Governor requests an extension of the liquidation date until June 30, 2014, for the $601,000 GF appropriation provided by Chapter 163, Statutes of 2006, for the costs of settlement in the case of *Vega et al. v. Richard Mallory*, California Department of Housing and Community Development (Sacramento County Superior Court, Case No. 97AS06548).

Background. The HCD Office of Migrant Services (OMS) provides safe, decent, and affordable seasonal rental housing and support services for migrant farmworker families during the peak harvest season through grants to local government agencies that contract with HCD to operate OMS centers located throughout the state. HCD obtains and administers funds for the construction and rebuilding of OMS centers

Chapter 163 provided the final funding for HCD to complete the repayment process prescribed by the *Vega v. Mallory* Settlement, which addressed overcharges by the OMS to center residents. The settlement provides that any remaining funds, after payment of all center resident claims, be used for OMS center repairs. However, the term of liquidation under Chapter 163 will expire before HCD can complete the process to utilize the remaining funds for OMS center repairs.

HCD reports that the court-appointed third-party settlement administrator did not notify HCD of the last payment being made in time for HCD to begin the process, as stated in the settlement, to utilize the remaining funds for OMS center repairs. Nonetheless, failure to use those funds for that purpose would be a violation of the settlement agreement by the HCD. This request would provide an extension to June 30, 2014, which is enough time for the OMS program to complete the process required through the settlement agreement as well as the usual repair process used by the state, thereby satisfying the requirements of the *Vega v. Mallory* settlement.

Staff Recommendation. Approve the May Finance letter.

Issue 4 – Federal Neighborhood Stabilization Program: Round 3

Governor's Request. In a May Revision Finance letter, the Governor requests approval for an increase in the Federal Fund Loan Assistance budget act authority of $11.3 million (federal funds) for the Neighborhood Stabilization Program, Round 3 (NSP3), as authorized by the Wall Street Reform and Consumer Protection Act of 2010. No additional authority is requested for state operations because HCD is reassigning staff to address this workload for the next five years.

Background. The federal NSP program is intended to assist states and local governments in the redevelopment of abandoned and foreclosed residential properties. The federal Department of Housing and Urban Development developed a formula for distributing funds based on the highest need resulting from home foreclosures. California received $145 million in Round 1 funding; HCD subsequently allocated those funds for statewide distribution. In Round 2, California localities received $314 million; HCD did not receive any funds in Round 2. Round 3 funding was restricted to areas of greatest need. HCD applied for and was granted $11.3 million in Round 3 federal funds to continue to manage and distribute funds to assist in solving California's problems of blighted neighborhoods.

HCD is reserving $590,000 of the total grant award for program administrative costs over the next five years. No additional budget authority is needed to because HCD expects to reassign existing staff to address the NSP3 workload; the position assigned to NSP1, where workload is declining, will move to the NSP3 as workload there begins to increase in 2011-12.

Staff Recommendation: Approve the May Finance letter.

DEPARTMENT OF MANAGED HEALTH CARE (2400)

For overview and budget information regarding this department, please see page 30 of this agenda.

Issue 1 – Federal Grant Funds

Governor's Request. In a May Revision Finance letter, the governor requests a reappropriation of $3.9 million in federal grant funds for activities to raise consumer awareness about federal health care reform and the Patient Protection and Affordable Care Act.

Background. In January 2011, the Joint Legislative Budget Committee (JLBC) approved $4.2 million federal funds expenditure for the Department of Managed Health Care (DMHC) to perform education and outreach activities to raise consumer awareness about federal health care reform. Due to delays in executing contracts for the provision of outreach and education services, DMHC will be unable to expend the entirety of the grant funds in the current fiscal year. This request is to allow DMHC to expend the remainder of the funds during the 2011-12 fiscal year.

DMHC intends to expend the grant funds for website design and content, translation services to provide consumer friendly access, enhancement of the communications system with upgraded hardware, and creating an online grievance/Independent Medical Review application that permits the efficient handling of increased consumer calls and complaint cases.

Staff Recommendation: Approve the May Finance letter.

COMMISSION ON STATE MANDATES (8885)

Department Overview: The Commission on State Mandates (Commission) is responsible for determining whether a new statute, executive order, or regulation contains a reimbursable state mandate on local governments and determining the appropriate reimbursement to local governments from a mandate claim. This budget item appropriates the funding for the staff and operations costs of the Commission, and appropriates non-education mandate payments to local governments. The Constitution, as amended by Proposition 1A of 2004, requires that the Legislature either fund or suspend local mandates – in most cases, if the Legislature fails to fund a mandate, the legal requirements are considered suspended pursuant to the Constitution. Payments for mandate costs incurred prior to 2004 are one exception noted in the Constitution, as are mandates related to labor relations.

Governor's January Budget Overview: The January Governor's Budget proposed expenditures of $56.7 million ($53.7 million GF) and 11.0 positions, a decrease of about $27.9 million over the adjusted current-year budget and no change in positions. It should be noted, the 2010-11 adjusted funding level is after the prior Governor's veto of $131 million. The Governor's budget includes the continuation of certain mandate suspensions, some new mandate suspensions, and deferrals of mandate payments to generate GF savings of about $321.7 million. The savings measures include: (1) savings of $94.0 million by deferring payment of pre-2004 mandate claims; (2) savings of $172.6 million by suspending certain local mandates; and (3) savings of $55.1 million from deferring payment on expired mandates or some mandates exempt from the requirements of Proposition 1A of 2004. Under (2) above, most mandates are proposed for suspension except those related to law enforcement and tax collection. Generally, the Governor proposed to fund only mandates related to law enforcement and local property tax collection.

March Budget Package: In March, the Legislature adopted a budget for the Commission similar to that proposed by the Governor ($53.7 million GF). However, in adopting the revised realignment package, the Legislature included a costs offset in another budget item for local law enforcement mandates, because those costs would be covered from new realignment revenues. The realignment action resulted in technical changes to the Commission on State Mandates item where those law enforcement mandates were deleted from the list of funded mandates.

May Revision: The Governor's May Revision includes several adjustments to the Commission on State Mandates Budget that result in a net GF cost reduction of $3.9 million.

Issue 1 – Conforming Changes for State Local Realignment

Governor's Request: In the May Revision, the Governor has modified his local realignment proposal to remove the $50.9 million associated with law enforcement mandates. To technically conform to this proposal, the mandates budget item needs to be modified to again list all the law enforcement mandates. Due to how this was budgeted in March with offsetting savings in another budget item, the $50.9 million is currently built into the mandates budget item and no changes are required to the level of appropriation.

Staff Comment: The public safety realignment proposal is primarily in the venue of Budget Subcommittee #5. Any changes by subject matter to the realignment package should be properly reflected in the budget for the State Mandate Commission.

Staff Recommendation: Conform the mandates budget to the final realignment package.

Issue 2 – Savings Based on State Controller's April 30 Report

Governor's Request: In the May Revision, the Governor requests a funding reduction of $3.9 million GF to reflect a revised cost estimate for law enforcement and property tax mandate reimbursements.

Staff Comment: The January budget is built on estimates of mandate claims, and the April State Controller report is updated for actual claims.

Staff Recommendation: Approve the May Revision request.

DEBT SERVICE GENERAL OBLIGATION BONDS & COMMERCIAL PAPER (9600)

Department Overview: Debt service payments are continuously appropriated, and therefore not appropriated in the annual budget bill. This item in the Governor's Budget displays the estimated debt service costs for each General Obligation bond (GO bond). Some bond costs are offset by special funds or federal funds – primarily by the transportation debt service fund. Other bonds are "self-liquidating," or have their own dedicated revenue (i.e., the Economic Recovery Bonds [ERBs] receive a quarter-cent of the sales tax) – the self-liquidating bonds are not included in this item.

January Governor's Budget Overview: The January Governor's Budget includes $4.9 billion in General Fund costs for GO debt service and related costs. In addition to this amount, $792 million in debt costs are funded from other funds (i.e., $778 million is from the Transportation Debt Services Fund that is associated with the truck-weight-fee proposal). Finally, federal bond subsidies, through the Build America Bonds (BABs) program, provide $351 million in 2011-12. The table below, with data from the January Governor's Budget, shows the three-year GO bond costs (in millions):

	2009-10 Actual Cost	**2010-11 Estimated Cost**	**2011-12 Estimated Cost**
General Fund cost	$4,639	$4,890	$4,927
Other funds cost	$239	$644	$792
Federal subsidy (Build America Bond Program)	$155	$300	$351
TOTAL Item 9600	**$5,033**	**$5,834**	**$6,070**
Economic Recovery Bonds (not included above)	$1,566	$1,351	$1,407

(see issue on next page)

Issue 1 – May Revision: New Estimates of Bond Debt Service

Governor's Proposal: As indicated above, funds for bond debt service are continuously appropriated and are considered one of the highest priorities for state expenditures. The Administration has new estimates for the cost of debt service in 2010-11 and 2011-12 that result in General Fund cost savings that total $267 million. One reason for the 2011-12 savings is that the Administration proposes to reduce its Fall 2011 bond sales from $5.8 billion to $1.5 billion. The Administration indicates that as of April 2011, total cash of $10.8 billion remains from prior bond issuances. So the new bond issuance of $1.5 billion would be sufficient to continue the bond program until a Spring 2012 issuance. The table below, with data from the Governor's Budget and May Revision, shows the three-year GO bond costs (in millions):

	2009-10 Actual Cost	**2010-11 Estimated Cost**	**2011-12 Estimated Cost**
January Budget General Fund cost	$4,639	$4,890	$4,927
May Revision Budget Adjustment	$0	-$140	-$126
Final Estimate of Cost	**$4,639**	**$4,749**	**$4,800**

Staff Recommendation: Approve the Administration's new cost estimate for GO bond debt service.

CASH MANAGEMENT AND BUDGETARY LOANS (9620)

Department Overview: This budget item appropriates funds to pay interest costs on General Fund borrowing used to overcome cash flow imbalances during the fiscal year. Because receipts and disbursements occur unevenly throughout the fiscal year, the General Fund borrows in most years, even though each budget is balanced when enacted and funds are repaid within the fiscal year. Interest is paid on both internal borrowing (such as cashflow loans from special funds) and for external borrowing (such as Revenue Anticipation Notes [RANs]). This item additionally pays interest costs for budgetary borrowing by the General Fund from special funds. Budgetary borrowing is across fiscal years and is scored as a budget solution, whereas cashflow borrowing is not counted as a budget solution (only a cash solution).

January Governor's Budget Overview: The January Governor's Budget included $300 million for interest costs on cashflow borrowing and $62 million for interest costs on budgetary borrowing – all General Fund. Of the cashflow amount, $100 million is for internal borrowing and $200 million is for external borrowing. Overall, expenditures in this item are up significantly – a total of $362 million is proposed for 2011-12, versus revised expenditures of $230 million in 2010-11. The year-over-year difference is primarily explained by the late budget last year that delayed the RAN sale until late in 2010. The Administration assumes the 2011-12 RAN sale will occur in July, resulting in a longer borrowing period and higher interest costs.

March Budget Action: The Legislature approved most of the Governor's cost assumption in the March budget package. An exception was that interest costs for special fund budgetary loans were reduced from $62.0 million to $57.7 million due to related budget action on special fund loans.

Issue 1 – Intra-year Payment Deferrals / Cashflow Loans

Governor's Proposal: The Administration has new estimates for the interest cost on special fund cashflow loans. The cost estimate is revised down from $100 million to $75 million in both 2010-11 and 2011-12. Estimated total GF savings over the two years totals $50 million.

Staff Recommendation: Approve the Administration's new cost estimates for special fund cashflow loans.

CAPITAL OUTLAY PLANNING AND STUDIES FUNDING (9860)

Issue 1 – Unallocated Capital Outlay Budget Reduction

Governor's Request. In a May Revision Finance letter, the Governor requests a decrease of $500,000 GF to reflect the reduction of the Unallocated Capital Outlay budget.

Background. The Unallocated Capital Outlay Budget provides funding to state agencies to develop design and cost information for new projects, known as "budget packages." The January Governor's Budget included $500,000 for these purposes in 2011-12. In prior years, the total funding provided was $1 million. This request would effectively zero out these funds in 2011-12.

Due to the current fiscal condition of the state, fewer infrastructure projects are being authorized and, as such, the state is preparing fewer budget packages. As a result, the Administration has determined that the $500,000 budgeted for 2011-12 is not needed because there are sufficient funds remaining for carryover from the 2010-11 appropriation. To the extent that it is determined that funds for budget packages are needed in 2012-13, it is anticipated that a request will be submitted through the normal budget process.

Staff Recommendation: Approve the May Finance letter.

LEASE REVENUE PAYMENT ADJUSTMENTS (CS 4.30)

Issue 1 – Various Lease-Revenue Bond Debt Service Adjustments

Governor's Request. In a May Revision Finance letter, the Governor requests various technical adjustments to amounts budgeted for lease-revenue debt service payments in 2011-12. The total of these changes is a decrease of $471,000 GF and a decrease of $4.047 million (other funds).

Background. Control Section 4.30 authorizes the Director of Finance to adjust amounts in appropriation items for rental payments on lease-purchase and lease-revenue bonds. In the case of the budgeted amounts for lease-revenue bond debt service in 2011-12, the decreases to the budgeted debt service amounts are a result of an update in the estimates of when bonds will be able to be sold.

Staff Recommendation: Approve the May Finance letter.

0840 STATE CONTROLLER

Department Overview. The State Controller is the Chief Fiscal Officer of the state. The primary functions of the State Controller's Office (SCO) are to provide sound fiscal control over both receipts and disbursements of public funds; to report periodically on the financial operations and condition of both state and local government; to make certain that money due the state is collected through fair, equitable, and effective tax administration; to provide fiscal guidance to local governments; to serve as a member of numerous policy-making state boards and commissions; and, to administer the Unclaimed Property and Property Tax Postponement Programs.

Budget Overview. The January Governor's Budget provides the SCO with 1,491 authorized positions and $218.9 million ($76.5 million GF). This is an increase of two positions and $65,000.

Issues Proposed for Discussion / Vote

Issue 1 – Local Government Oversight Initiative (April Finance Letter and May Revision Finance Letter)

Governor's Request. In an April Finance Letter, the Governor requests increased expenditure authority of $2.098 million (reimbursements) to support 16.4 existing positions to provide increased oversight of local government entities under the SCO's existing statutory authority.

In a separate May Revision Finance letter, the Governor requests increased expenditure authority of $1.44 million (GF) and ongoing to support 11.8 positions for increased oversight of local government entities under the SCO's existing and proposed statutory authorities.

Prior Subcommittee Action. The April Finance letter was held open at the Subcommittee's May 5, 2011, hearing, pending receipt of a systematic plan from the SCO detailing how the SCO would execute the additional activities, as well as an audit plan and a benefit/cost assessment of the additional financial monitoring.

Background. Generally speaking, direct state oversight of local governments is currently limited to state and federal pass-through funding. Counties receive a large share of state/federal pass-through funding to administer a number of statewide programs under state supervision, such as health and welfare. As a result, they receive direct state oversight, including SCO audits. For cities and special districts, state oversight is more limited to the few grants or allocations of state/federal pass through funding, such as Gas Tax allocations, distributed by the state. In addition, current statute provides for a more indirect oversight of local government funding using the following three elements:

1. Annual Audits. Each local government entity is required to have an annual audit performed by an independent auditor. If the local government has over $500,000 in federal expenditures, it must also have a single audit. Local governments are required to submit these single audits to the SCO.
2. Financial Transaction Reports. Statute requires the SCO to collect a report of annual financial transactions from each county, city, and special district and to publish them in

reports available to the Governor, legislature, and general public. Statute further provides that, if the reports are not made in the time, form, and manner required, or if there is reason to believe a report is false, incomplete, or incorrect, the SCO shall appoint a qualified accountant to make an investigation and to obtain the information required. Statute specifies that the SCO's enforcement costs are to be reimbursed by the local government entity in question. Statute also specifies that the Controller can impose financial penalties for late filing (or failure to file) of a financial transaction report by a local government entity. The penalties range from $1,000 to $5,000, dependent the total revenue of the government entity. On average, approximately $251,000 in such penalties is invoiced each year with approximately $100,000 received, which is then deposited into the GF.

3. Accounting and Audit Guidelines. Uniform accounting guidelines are intended to provide local governments with the information necessary to implement and operate a common accounting and reporting system. Currently such guidelines are only required for counties and special districts.

With regard to the financial transaction reports, these reports represent the only source of available statewide financial data on local government entities. According to 2010 estimates, the SCO staff spent more than 1,100 hours annually on monitoring the submissions and collecting forfeitures (required payments to the state for failure to file the financial report with the SCO). The SCO indicates that the reports are subject to automated edits that do not necessarily identify all the issues that warrant attention. For instance, the SCO does not presently have the resources to compare these reports between years or between similar entities. In addition, the current analyses of all of the complaints that are being submitted to the SCO (since the City of Bell stories were reported last year) are being done through staff redirections. To the extent that an analysis results in a need for further investigation, additional redirections would be needed.

Staff Comment. The current approach is not working at an optimal level to protect taxpayers from waste, fraud, and abusive financial practices. In response, the SCO has developed a Local Government Oversight Initiative, which is intended to increase oversight of local government financial matters. There is merit in increasing oversight, as most state money is spent at the local level.

As noted above, the SCO's initiative is presented in two requests. The April Finance letter consists of using the SCO's existing statutory authority to expand oversight and utilizing reimbursements from local governments to fund the SCO's costs. More specifically, this request would rely on increased expenditure authority of $2.1 million (reimbursements) to support 16.4 positions on an ongoing basis. This request focuses on the financial transaction reports detailed above and would provide resources to the SCO to investigate and prepare annual financial transaction reports for all non-filers, as well as conduct investigations of individual financial issues that indicate some information in an annual transaction report is "false, incorrect, or incomplete." However, as noted in the SCO's submitted audit plan, "the only way to determine the precise level of workload is to actually perform it." This raises questions about the long-term level of workload, as well as whether the SCO will be able to secure sufficient reimbursements. Failure to secure sufficient reimbursements would put the GF at risk for being the fund source to support these activities. Therefore, in considering this request, the Subcommittee may wish to: (1) reduce the resources by half; (2) make the approval three-year limited-term; and (3) adopt placeholder supplemental report language to require an annual report documenting the level of effort and findings and outcomes, to ensure that the

Subcommittee has a future opportunity to revisit this initiative and ensure desired outcomes are being achieved.

With regard to the May Revision Finance letter, this request proposes a mix of current and proposed statutory authority (the SCO is sponsoring two pending bills) to increase oversight by: (1) increasing the types of audits of local government that are submitted to the SCO; (2) increasing the number of quality control reviews of audits of local government; (3) posting all local government audits to, and establishing a "dashboard" of information on each city, county, and special district on, the SCO's website; (3) increasing the current penalties for failure to file annual transaction reports; and (4) expanding the collection and reporting of local government compensation data to include all local government entities. This request would rely on new GF spending of $1.44 million to support 11.8 positions on an ongoing basis. As noted above, it is not clear that the workload here is ongoing and sustainable. Further, the SCO is sponsoring two bills, AB 229 (Lara) and AB 276 (Alejo), to make the statutory changes necessary for the SCO to carry out the new duties under this request as well as increase the penalties. As such, and in considering this request, the Subcommittee may wish to defer to the policy process and then consider any requests to further expand the SCO's local government oversight activities once the bill process has concluded and as part of the 2012-13 budget process in January of next year.

Staff Recommendation:

- **April Finance letter**: Approve the April Finance letter as modified: (1) three-year limited-term basis $1.049 million (reimbursements) to support 8.2 existing positions and (2) placeholder supplemental report language requiring the SCO to report annually on its level of effort and findings and outcomes related to increased oversight of local government finances.

- **May Finance letter**: Reject the May Finance Letter and defer to legislative policy process.

Vote: Staff recommendations on both April Finance and May Finance letters approved by a vote of 3-0.

Issue 2 – Unclaimed Property Holder Compliance Initiative

Governor's Request. In a May Revision Finance letter, the Governor requests increased expenditure authority of $2.414 million (Unclaimed Property Fund - UPF) and 22.6 positions for 2011-12 ($2.442 million and 23.6 positions in 2012-13; $2.438 million and 23.6 positions in 2013-14 and ongoing) to develop and implement a holder outreach and compliance program to identify and contact non-reporters or inconsistent reporters of unclaimed property and bring them into compliance with the Unclaimed Property Law.

Related 2011-12 Budget Action. As part of the March 2011 Budget package, the Legislature approved the following related to the Unclaimed Property Program: (1) $293,000 (UPF), one permanent and 3.1 two-year limited term positions, for support of increased accounting workload; and (2) a two-year augmentation of $300,000 (UPF) for unclaimed property legal costs.

Background. Under the Unclaimed Property Law (UPL), the SCO is responsible for safeguarding unclaimed property until it is returned to its rightful owner. The UPL was enacted to ensure that property is returned to its rightful owner(s) and to prevent holders of unclaimed property from transferring it into their business income. Holders of unclaimed property must report and remit unclaimed property to the SCO after a specified period of time. In 2009, the SCO Division of Audits issued its first ever comprehensive analysis of holder compliance with the UPL by using Franchise Tax Board audits. The analysis identified 1.3 million active California-based businesses, of which at least 1,238,000 did not file an unclaimed property report with the SCO. The SCO believes that 34.5 percent of those filers are not required to file; of the remaining 851,000 businesses the SCO currently only receives 17,000 reports on an annual basis for a compliance rate of two percent. The SCO presents that a larger holder outreach unit would allow the SCO to contact non-compliant entities to bring them into compliance with the UPL. Of the 22.6 positions requested, 5.3 would be for outreach activities.

The SCO is also requesting to expand the audit activities under the Program, including desk reviews of businesses that have been audited to ensure they are still reporting on a yearly basis, and desk reviews of other businesses that have reported in the past to ensure they are reporting consistently. Of the 22.6 positions requested, 17.3 would be for audit activities.

The SCO estimates that this initiative will reunite owners with an estimated $113 million of their property over the next five years. Over the same five-year period, the increased efforts will result in remittance of approximately $136 million to be held in perpetuity for owners to claim. The SCO indicates that its initiative is self-funded and is estimated to result in net receipts to the GF in 2011-12 of $16.8 million, including $9.7 million from holder penalty and interest.

Staff Comment. In prior years, the SCO performed approximately 50 audits per year of unclaimed property holders within California. That audit work was reduced due to a budget reduction to the Unclaimed Property Program. To absorb those reductions, the SCO focused on work to return property to its rightful owner(s), as that is the goal of the program. Without an audit presence, the risks to holders for non-compliance diminish.

Staff Recommendation: Approve the May Finance letter.

Vote: Staff recommendation approved by a 3-0 vote.

0845 DEPARTMENT OF INSURANCE

Department Overview. The California Department of Insurance (CDI) regulates the California insurance market and enforces the California Insurance Code, conducting examinations and investigations of insurance companies and producers and working to ensure the financial solvency of companies so that they will meet their obligations to policyholders and claimants. CDI investigates more than 300,000 complaints annually and responds to consumer inquiries. CDI also reviews and approves insurance rates to enforce the statutory requirement that rates are not excessive or unfair. CDI also administers the conservation and liquidation of insolvent and delinquent insurance companies and fights insurance fraud in conjunction with local and state law enforcement agencies.

Budget Overview. The January Governor's Budget provides CDI with 1,338 authorized positions and $224.94 million (Insurance Fund and reimbursements). This is an increase of 71 positions and $16.4 million.

Issue Proposed for Discussion / Vote

Issue 1 – Federal Health Care Reform: Additional 2011-12 Positions

Governor's Request. In a May Revision Finance letter, the Governor requests an increase of $748,000 (Insurance Fund) ongoing for eight existing positions to address the increased workload associated with defining and implementing federal health care reform (Patient Protection and Affordable Care Act – PPACA).

Prior 2011-12 Budget Actions. The Legislature approved earlier this year, as part of the March budget package, a total of 71 positions and $9.8 million (Insurance Fund) for the CDI, as follows:

2011-12 Funds	Positions	Function	Chapter Citation
$1,200,000	10 (9 2-year limited term and 1 1-year limited term)	PPACA and additional workload associated with the review of health insurance rate filings.	Chapter 661, Stats of 2010 (SB 1163)
$642,000	6 staff counsel, all 2-year limited-term	PPACA, additional rate filings, and new cancellation and non-renewal appeal process.	Chapter 658, Stats of 2010 (AB 2470)
$107,000	1 staff counsel, 2-year limited-term	PPACA and additional policy form review activities required as a result of the implementation of the California Health Benefits Exchange.	Chapters 659 and 655, Stats of 2010 (SB 900 and AB 1602, respectively)
$8,000,000	54 positions, permanent	Increased workload and to meet statutory mandates.	No change in statute cited.

Background. On March 23, 2010, President Obama signed the PPACA into law, a comprehensive health reform proposal intended to expand coverage, control health care costs, and improve the health care delivery system. The PPACA makes several fundamental changes to the private health insurance market, including setting up a new competitive private health insurance market through state Exchanges beginning in 2014, and prohibitions on lifetime benefit coverage limits and rescissions of coverage. In 2010, several state statutory changes were enacted to align California law with the new federal mandates under the PPACA. These statutory changes drove the 2011-12 budget requests summarized in the above chart.

The CDI requests these additional resources to implement PPACA for the following purposes: (1) providing expertise and consultation regarding legal and implementation issues to various CDI units; (2) legal consultation regarding proposed legislation; and (3) implementation of new legislation, policy monitoring, analysis, and recommendation regarding current and future impacts of health reform on CDI. Additionally, there will be workload associated with the coordination of future implementation activities with the Legislature, the Governor, the U.S. Department of Health and Human Services, and the National Association of Insurance Commissioners (NAIC), as well as mandated reporting requirements. The positions requested are as follows:

Positions	Classification	Funding
1.0	Associate Health Program Advisor	78,000
2.0	Health Program Specialist I	173,000
1.0	Health Program Specialist II	96,000
4.0	Staff Counsel	401,000
	TOTAL	**748,000**

LAO Recommendation. We recommend the Legislature reject the May Revision request for $748,000 in special funds to pay for eight currently authorized positions. Our analysis finds that the department has funding for 17 staff that is in excess of the level of resources justified on a workload basis. The department can redirect funds to pay for the eight positions.

Staff Comment. Unlike the regulatory adoption process here in California, PPACA devolved certain responsibilities for the regulatory process to the NAIC. Therefore, staff concurs that it is critical for the California Insurance Commissioner and key staff representatives to participate in NAIC activities related to the development of model laws and regulations for PPACA.

However, while the function of the eight positions being requested here is different from the Subcommittee's prior 2011-12 actions, these positions are proposed as permanent whereas the 17 PPACA-positions already approved are all limited-term. In discussions with staff, the CDI could not provide a clear explanation as to why these eight positions are proposed as permanent. In addition, post Subcommittee approval of the 54 position request earlier this year, the LAO was able to finalize its workload analysis of that request. The analysis found that of the 54 positions approved, 17 positions were unjustified.

Therefore, in considering this request, the Subcommittee may wish to consider not approving the request for increased expenditure authority and instead direct the CDI to absorb the workload within the January budget request. With 17 of those 54 positions determined to not be justified by the workload, there is ample capacity to absorb the workload in this May Revision request.

In either case, the Subcommittee may also wish to make any action here approved on a two-year limited-term basis, to ensure that all positions at CDI related to PPACA "cycle off" in two years' time to allow a full review of the workload and ensure the appropriate budget resources are provided. This is especially important because the full extent of the workload related to PPACA and changes in statute is not fully known.

Staff Recommendation: Deny the request for increased expenditure authority, and instead direct the Department of Insurance to absorb the workload in this request within the previously approved 54 positions.

Vote: Staff recommendation approved by a vote of 2-1 with Senator Evans voting no.

The Chair requested that the Department present updated workload information in January of 2012.

0911 CITIZENS REDISTRICTING COMMISSION

Issue Proposed for Discussion / Vote

Issue 1 – Citizens Redistricting Commission Continuing Activities

Governor's Request. In a May Revision Finance letter, the Governor requests that $400,000 GF be added to the 2011-12 budget to provide additional resources necessary for the Citizens Redistricting Commission (Commission) to complete the required redistricting maps by the constitutional deadline of August 15, 2011, and to perform related support activities. In addition, the Governor requests that provisional budget bill language be added to allow the Commission access of up to $1.5 million GF for litigation support activities in 2011-12.

Background. Proposition 11, the Voters FIRST Act, was approved by the voters on the November 4, 2008, General Election Ballot. Proposition 11 changed the state's redistricting process by establishing a 14-member Citizens Redistricting Commission (Commission) to draw the new district boundaries for the State Assembly, State Senate, and Board of Equalization beginning with the 2010 Census and every ten years thereafter. Proposition 11 specifies that a minimum of $3 million in funding be provided, or the amount appropriated for the previous redistricting plus the Consumer Price Index, whichever is greater.

Per the requirements of Proposition 11, the 2009-10 Budget appropriated $3 million GF for Proposition 11 implementation costs over a three-year period for the Commission, State Auditor, and Secretary of State. Additionally, the 2010-11 budget included provisional budget bill language to provide an expedited request process should the Commission demonstrate it required funding greater than the $2.5 million (amount that remained from the 2009-10 $3 million GF appropriation) for its costs from January 1, 2011, to June 30, 2011.

Proposition 20 was approved by the voters on the November 2, 2010 General Election Ballot, requiring changes and expansions to the 2008 amendments to the California Constitution. The 2010 amendments added California's 53 Congressional Districts to the Commission's redistricting responsibilities and expanded the criteria for the district mapping process. The amendments also shortened the completion date for all four maps and supporting reports to no later than August 15, 2011, thereby reducing the time allowed for the Commission's mandatory submission of the four maps to the Secretary of State by one month. These amendments were made with no additional appropriation of funds to support the expanded responsibilities and requirements.

In May 2011, the Joint Legislative Budget Committee approved the $1 million GF available through the 2010-11 budget provisional language. The Commission reports that it will have expended the entirety of the available funds by the end of 2010-11.

Staff Comment. The Commission has made a compelling case for the need for additional funds in the amount of $400,000 GF to complete its mandated work by the August 15, 2011, deadline. The proposed provisional budget bill language is similar to the approach taken in 2010-11, whereby there were some unknowns about the Commission's workload but a need for the Commission to have an expedited process and access to additional funds upon demonstrated need. At this point, it is not certain that litigation will be filed challenging the certified maps, but it would be wise to plan for that contingency. However, it is also important to not over appropriate this budget item; under the terms of Proposition 11, the total funding provided to this item creates a permanent baseline GF funding amount adjusted for inflation in future years. The Administration's May Revision proposal strikes the right balance to ensure this effort is appropriately and adequately funded.

Staff Recommendation: Approve the May Finance letter.

Vote: Staff recommendation approved by a 3-0 vote.

2400 DEPARTMENT OF MANAGED HEALTH CARE

Department Overview. The Department of Managed Health Care (DMHC) was established in 2000, when the licensure and regulation of the managed health care industry was removed from the Department of Corporations and placed in a new, stand-alone, department. The mission of DMHC is to regulate, and provide quality-of-care and fiscal oversight for Health Maintenance Organizations (HMOs) and two Preferred Provider Organizations (PPOs). These 94 Health Care Plans provide health insurance coverage to approximately 64 percent of all Californians. Recent statutory changes also make DMHC responsible for the oversight of 240 Risk Bearing Organizations (RBOs), who actually deliver or manage a large proportion of the health care services provided to consumers. Within the Department, the Office of the Patient Advocate helps educate consumers about their HMO rights and responsibilities.

Budget Overview. The January Governor's Budget provides DFI with 250.2 authorized positions and $35 million (no GF). This is an increase of 2.7 positions and $55,000 over 2010-11.

Issue Proposed for Discussion / Vote

Issue 1 – Consumer Participation Program Sunset

Governor's Request. The Governor has no request.

Background. The Consumer Participation Program is housed within DMHC. Under this program, the DMHC Director may award advocacy and witness fees to a person or organization which represents the interests of consumers and has made a substantial contribution on their behalf to the adoption of a regulation, Director's order or decision affecting a significant number of consumers. The Director may identify regulatory proceedings in which he or she believes consumer participation would be helpful and anticipates that fees may be awarded. A person or organization desiring to participate in a proceeding and seek an award of fees will submit a *Petition to Participate in a Proceeding*. Current statute sets the total amount of compensation annually at $350,000. Similar programs currently exist at the Public Utilities Commission and at the Department of Insurance.

Staff Comment. It is important to note that the organizations receiving compensation are not being paid to advocate for consumers, they are being paid to inform the rulemaking process and to represent the experience of consumers with regard to what they have learned as they advocate.

Staff Recommendation: Approve trailer bill language to extend the Consumer Participation Program sunset until January 1, 2018.

Vote: Staff recommendation approved by a 2-1 vote with Senator LaMalfa voting no.

8885 STATE MANDATES

For additional background on the Commissions on State Mandates, including their total budget, please see the write-up in the vote-only section of the agenda.

Issues Proposed for Discussion / Vote

Issue 1 – Local Agency Formation Committees (LAFCO) Mandate

Governor's Request: In the May Revision, the Administration proposes: (1) to increase budget funding by $277,000 GF to reflect recent action by the Commission on State Mandates to adopt cost estimates for the LAFCO mandate; and (2) to suspend the LAFCO mandate and delete funding of $277,000 (payment would still be due in a future year) . The "LAFCO mandate" is a small part of LAFCO law – specifically, the requirement that special districts file written statement to LAFCOs specifying the functions of classes of service proved by those districts.

Constitutional Requirements: Proposition 1A of 2004 amended Section 6 of Article XIII B of the State Constitution to require that reimbursement claims from local governments either be paid, or that the mandate be suspended or repealed. So the State must either pay the LAFCO mandate in this budget, or suspend or repeal the requirements for 2011-12 to defer payment of the $277,000.

LAO Recommendation: The LAO recommends the Legislature adopt trailer bill language that would have the technical effect of repealing the LAFCO mandate. Repeal would simply *authorize*, instead of *require*, LAFCOs to direct special districts to file these statements. Since LAFCOs could still require the special districts to report, overall effect on the program should be none or minor. Other requirements of the LAFCO program would remain unchanged. With the LAO recommendation, the state would not have to pay the cost of this activity in future years, but the State will eventually have to pay the $277,000 for past claims.

Staff Recommendation: Approve the LAO trailer bill language.

Vote: Staff recommendation approved by a 3-0 vote.

Issue 2 – Local Government Employment Relations Mandate

Governor's Request: In the May Revision, the Governor proposes: (1) to increase budget funding by $4.9 million GF to reflect recent action by the Commission on State Mandates to adopt cost estimates for the LGEF mandate; and (2) to defer payment of the LGEF mandate and delete funding of $4.9 million (payment would still be due in a future year). This mandate requires local governments to respond to charges of unfair labor practices made to the Public Employment Relations Board and deduct union dues from certain employees' paychecks.

Constitutional Requirements: Proposition 1A of 2004 amended Section 6 of Article XIII B of the State Constitution to require that reimbursement claims from local governments either be paid, or that the mandate be suspended or repealed. However, labor-relations mandates are specifically excluded from this requirement and payment can be deferred without suspension or repeal of the mandate. The Governor's proposal is to defer payment of the $4.9 million General Fund to an unspecified out-year and to keep the mandate requirements on local governments in place.

LAO Recommendation: The LAO recommends approval of the Governor's proposal to defer payment of the mandate. The LAO notes that the implementing legislation did not anticipate these State costs, and that in light of this, the relevant policy committee should again review these requirements.

Staff Recommendation: Approve the May Revision request.

Vote: Staff recommendation approved by a 3-0 vote.

8940 MILITARY DEPARTMENT

Department Overview. The California Military Department (CMD) is responsible for the command, leadership, and management of the California Army and Air National Guard and five other related programs. The CMD is organized in accordance with federal Departments of the Army and Air Force staffing patterns. In addition to the funding that flows through the State Treasury, the CMD also receives Federal Funding directly from the Department of Defense.

Budget Overview. The January Governor's Budget provides the CMD with 854.5 authorized positions and $144.3 million ($46.0 million GF). This is a decrease of 11.0 positions and an increase of $3.8 million ($1.1 million GF).

Issue Proposed for Discussion / Vote

Issue 1 – Reduce Military Retirement Program

Governor's Request. In a May Revision Finance letter, the Governor requests a decrease of $1.5 million GF and two positions to reflect a reduction in retirement benefit costs provided to eligible retired service members. The CMD has since requested to maintain $300,000 of that savings and the two positions for an expansion of the California Cadet Corps.

Background. The CMD's Retirement Program (Program 40) was established prior to the CMD's participation in the California Public Employees Retirement System (CalPERS). Program 40 provides services similar to those provided by the federal military, to persons who entered State Active Duty (SAD) prior to October 1, 1961, and have served 20 or more years, at least 10 of which have been on SAD, or have been separated for physical disability. All other permanent civil service employees have been and are covered by CalPERS. Program 40 currently provides coverage for 29 individuals (12 retirees and 17 survivors of retirees).

The CMD indicates that when the SAD personnel hired after October 1, 1961, entered PERS, the monthly payroll was done as a manual hand-typed payroll submitted to the State Controller's Office (SCO). The CMD was responsible for calculating pay and all employer costs. When the checks were received from the SCO, the CMD was responsible for releasing the warrants for CalPERS, taxes, medical, Social Security, and Medicare. At the time, the SCO did not have a system that could calculate the military pay. In the 1990's, the CMD and the SCO were finally able to get the SAD personnel on the SCO payroll system. The retirement payroll in Program 40, which also was, and still is, a manual system done by the CMD, was not combined due to the fact that the employees on this payroll never paid into CalPERS and the SCO does not have a system that would enable the CMD to transfer this manual payroll. As the direct costs for Program 40 have gone down over the years due to retiree and or survivor deaths, the distributed portion of the program has not been reduced or reallocated to other programs. This request aligns the funding with the program costs.

The mission of the California Cadet Corps is to provide California schools and students with a quality educational and leadership development program that prepares students for success in college and the work force. The funding and positions retained for the Corps expansion will fund two positions to expand the Corps by 1,000 cadets (currently there are 4,400).

Staff Recommendation: Approve the May Finance letter, as modified by the CMD's subsequent request related to the Cadet Corps expansion. With regard to the resources for the Cadet Corps, staff recommends approval on a two-year limited-term basis with placeholder supplemental report language requiring the CMD to report annually on expenditures and outcomes.

Vote: Staff recommendation approved by a 3-0 vote.

8955 CALIFORNIA DEPARTMENT OF VETERANS AFFAIRS

Department Overview. The California Department of Veterans Affairs (CDVA) promotes and delivers benefits to California veterans and their families. More specifically, the CDVA provides: (1) California veterans and their families with aid and assistance in presenting their claims for veterans' benefits under the laws of the United States; (2) California veterans with beneficial opportunities through direct low-cost loans to acquire farms and homes; and (3) the state's aged and disabled veterans with rehabilitative, residential, and medical care and services in a home-like environment at the Veterans Homes of California (VHCs). The CDVA operates VHCs in Yountville (Napa County), Barstow (San Bernardino County), Chula Vista (San Diego County), and Greater Los Angeles Ventura County (with homes in West Los Angeles, Ventura, and Lancaster).

Budget Overview. The January Governor's Budget proposes to continue to ramp-up admissions at the VHCs in West Los Angeles, Lancaster, and Ventura. The Governor also proposes to provide continued resources and staffing related to the construction and activation of two new VHCs, in Redding and Fresno, both of which are scheduled to begin admissions in early calendar year 2012. The January Governor's Budget provides CDVA with 2,396.5 authorized positions and $399.3 million ($253.4 million GF).

The construction cost of the VHCs was/is funded with $50 million in general obligation bonds available through Proposition 16 (2000), an estimated $212 million in lease-revenue bonds [most recently amended by Chapter 824, Statutes of 2004 (AB 1077)], and federal funds.

Issue Proposed for Discussion / Vote

Issue 1 – Program 30: Veterans Homes of California, Greater Los Angeles Ventura County

Background. The CDVA provides residential and medical care services to honorably discharged California veterans who served on active duty and are over the age of 62 or disabled. The VHCs are long-term residential care facilities that provide California's qualified aged or disabled veterans with rehabilitative, residential, medical, and support services in a home-like environment. Once an eligible veteran selects a VHC as his or her long-term care option, and is approved for admission, the veteran becomes a fee paying resident of the VHC. Spouses of veterans may also be eligible for VHC membership. The VHCs provide a long-term continuum of care, from domiciliary care at one end of the spectrum, which is similar to independent living accommodations, to skilled nursing care at the other end of the spectrum, which provides continuous skilled nursing or rehabilitation services.

March 2011 Budget Package. As part of the March 2011 Budget package, the following resources were approved for the VHCs in 2011-12:

- Net GF increase of $31.7 million for all of the VHCs, including: (1) an augmentation of $24 million for full-year and one-time adjustments to phase-in staffing and residents in the existing and new VHCs in Greater Los Angeles Ventura County (GLAVC), Redding, and Fresno; (2) $4.7 million for furlough and personal leave program reductions which are only reflected in the 2010-11 fiscal year budget; and (3) $9.3 million in increased lease-revenue bond payments for VHC-GLAVC. The expenditures are offset by an increase of $5.0 million in GF revenue.

This funding level is $8.1 million below the Governor's January budget, reflective of savings resulting from: (1) a three-month delay in the opening of the Redding and Fresno VHCs; and (2) the staggered opening of the Residential Care for the Elderly (RCFE) and Skilled Nursing Facility (SNF) levels of care at the Redding and Fresno VHCs. The opening of the Redding home will be delayed from February 2012 to May 2012; the opening of the Fresno home will be delayed from April 2012 to July 2012. In both homes, SNF residents will be admitted in January 2013. The total savings from these combined actions is $8.9 million GF; however, the reduction of offsetting revenue (federal per diem subsidies and resident fees) of $800,000 reduces the overall savings to the $8.1 million GF figure noted above.

Staff Comment. When the Subcommittee acted on Program 30 earlier this year it stated intent to reopen the VHC budget in Spring 2011 when caseloads were known to make any necessary adjustments to the 2011-12 budget to account for salary savings because not all of the positions contained in the request would be hired per the schedule. Given the action to delay the opening of the Redding and Fresno VHCs, the question before the Subcommittee is whether there is any salary savings within the GLAVC VHC request.

The chart below illustrates the resident census at the GLAVC facilities at two points in 2010-11 as compared to the census goal for 2010-11:

VHC	January 17, 2011 Census	May 17, 2011 Census	2010-11 Census Goal
West Los Angeles	21	40	39
Lancaster	22	41	54
Ventura	39	52	54

While the above chart illustrates that the Ventura and West Los Angeles VHCs are on track to reach their 2010-11 census goal, in the case of the Ventura facility that goal was originally estimated to be met in September 2010. In the case of the Lancaster VHC, while significant progress has been made since January to increase resident admissions, that facility is unlikely to reach its target, a target that was originally estimated to be reached in August of 2010.

Given these factors, it is quite likely that there is salary savings in the 2010-11 budget due to the pace of admissions at the GLAVC facilities and the admission level at VHC-Lancaster. Any GF savings in the current year will revert at the end of year automatically, but staff notes that adjustments should potentially be made to the 2011-12 GLAVC budget to account for salary savings, if identified. The LAO is working with the DOF and CDVA, but given time constraints of the May Revision, the final analysis was not complete at the time this agenda was written.

The LAO will present information to the Subcommittee at today's hearing as to its findings.

Staff Recommendation: To the degree salary savings (GF) are identified within the 2011-12 budget for the GLAVC VHC, staff recommends adoption of the LAO's findings.

Vote: Subcommittee approved by a 3-0 vote a net $6.1 million GF reduction in 2011-12 as follows: (1) reduce Item 8955-001-0001 by $7.38 million; (2) reduce Item 8951-501-0001/8951-501-0890 by $853,000; and (3) other GF revenues reduced by $467,000.

9620 CASH MANAGEMENT AND BUDGETARY LOANS

For additional background on Cash Management and Budgetary Loans, please see the write-up in the vote-only section of the agenda.

Issue Proposed for Discussion / Vote

Issue 1 – Accelerate Repayment of Special Fund Loans

Governor's Proposal: In the May Revision, the Administration proposes to accelerate repayment of $744 million in special fund loans from 2012-13 into 2011-12. Since these loans are repaid from the General Fund, this proposal is a "negative" budget solution, or a budget hit to 2011-12. However, the Governor proposes this action to begin paying off budgetary borrowing that he pegs at $34.7 billion. Among the largest categories of budgetary borrowing are deferrals to K-12 schools and community colleges ($10.4 billion), outstanding Economic Recovery Bonds ($7.1 billion) and loans from special funds ($5.1 billion). So the May Revision proposal would reduce outstanding special fund loans from $5.1 billion to $4.4 billion. The specific loan repayments are listed below.

Loans to be Repaid in 2011-12 (were due in 2012-13)
2011-12 May Revision
(Dollars in Thousands)

Org	Dept	Fund Title	Fund	Amounts
0502	OSCIO	State Emergency Telephone Number Acct	0022	$28,000
1111	DCA	Enhanced Fleet Modernization subaccount	3122	40,000
1110	DCA	Accountancy Board	0704	173
3360	CEC	Renewable Resources Trust Fund	0382	18,200
3360	CEC	Renewable Resources Trust Fund	0382	10,900
3360	CEC	Renewable Resources Trust Fund	0382	35,000
3360	CEC	Alternative and Renewable Fuel and Vehicle Technology Fund	3117	8,250
3360	CEC	Alternative and Renewable Fuel and Vehicle Technology Fund	3117	16,300
3500	DRRR	Beverage Container Recycling Fund	0133	72,277
3500	DRRR	Beverage Container Recycling Fund	0133	99,400
3500	DRRR	Electronic Waste Recovery & Recycling	3065	80,000
3560	SLC	School Land Bank Fund	0347	59,000
3680	DBW	Harbors and Watercraft Revolving Fund	0516	29,000
3790	Parks	Off-Highway Vehicle Trust Fund	0263	90,000
4140	OSHPD	Hospital Building Fund	0121	20,000
4140	OSHPD	Health Data and Planning Fund	0143	12,000
8120	POST	Peace Officers' Training Fund	0268	5,000
8660	PUC	High-Cost Fund-B Administrative Committee Fund	0470	44,000
8660	PUC	High-Cost Fund-B Administrative Committee Fund	0470	15,000
8660	PUC	Teleconnect Fund	0493	61,800
		Total		**$744,300**

Staff Recommendation: Approve the Governor's proposal to start paying down budgetary borrowing.

Vote: Staff recommendation approved by a 3-0 vote.

REDUCING STATE GOVERNMENT

Background. The March 2011 budget package recognized $250 million GF ($163 million other funds) for savings associated with the identification of efficiencies in state operations, including identification of agencies, departments, and programs that can be reorganized to eliminate duplication and unnecessary functions; review of state peace officer and safety classifications; and reductions in other areas like contracting, fleet operations, and cell phone use. The mechanism to achieve these savings is a budget control section that provides the Administration with the authority to make the required budgetary reductions to achieve the total savings.

Working from these totals, the Administration has since identified, and in some cases already achieved, savings through a variety of executive actions, including eliminating the offices of the Secretary of Education and the American Recovery and Reinvestment Act Inspector General, banning non-essential travel, implementing a statewide building rental rate reduction, reducing the number of state-issued cellular phones, and reducing the statewide vehicle fleet, including the elimination of any non-essential vehicles and reducing the number of home-storage permits.

The May Revision builds on these executive actions and proposes to specifically reduce state operations by $82.7 million ($41.5 million GF) via the same control section mechanism included in the March 2011 budget package. These savings would be achieved through a variety of eliminations, consolidations, reductions, and efficiencies, including: (1) the elimination of 32 boards, commissions, task forces, and offices; (2) the consolidation of the State Personnel Board and the Department of Personnel Administration; (3) several changes due to realignment, including the elimination of the Departments of Mental Health and Alcohol and Drug Programs and a 25 percent state operations reduction for realigned public safety programs; and (4) various program reductions and efficiencies. The May Revision proposal also includes a comprehensive state asset review to result in the eventual disposition of non-essential or under-utilized state properties; however, any savings from this effort would be included in the 2012-13 budget.

All of the proposed eliminations and consolidations, to the degree that they require statutory changes, cannot be adopted on an urgency basis. Article 4, Section 8 (d), of the California State Constitution states that, “an urgency statute may not create or abolish any office or change the salary, term, or duties of any office, or grant any franchise or special privilege, or create any vested right or interest.” Therefore, the eliminations and consolidations all have an effective date of January 2, 2012, with the associated savings of six months.

Control Sections 3.91 and 13.25, entitled “Reductions in State Operations” and “Reorganizations and Consolidations,” respectively, are in the purview of this Subcommittee and discussed further below. In addition, also discussed below are the specific “Reducing State Government” proposals that fall within the jurisdiction of this Subcommittee. The remaining items are being addressed by the relevant Senate Budget Subcommittee with jurisdiction.

Issues Proposed for Discussion / Vote

Issue 1 – CS 3.91 Reductions in State Operations and CS 13.25 Reorganizations and Consolidations

Governor's Request. In a May Revision Finance letter, the Governor requests revisions to CS 3.91, pertaining to reductions in state operations, which was approved as part of the March 2011 Budget package. These revisions provide additional specificity regarding departmental consolidations, operational efficiencies, and other cost reduction measures.

In addition, and in a separate May Revision Finance letter, the Governor requests that a new control section be added to the 2011-12 budget, CS 13.25 entitled Reorganizations and Consolidations to reflect reorganizations and consolidations of departments or functions of departments that are approved by the Legislature.

Background. The Budget Act is divided into sections. Section 1.00 establishes a citation for the legislation. Section 1.50 provides a description of the format of the act. Section 2.00 contains the itemized appropriations. Sections 4.00 through 99.50 are general sections, also referred to as control sections, which generally provide additional authorizations or place additional restrictions on one or more of the itemized appropriations contained in Section 2.00.

CS 3.91, as approved as part of the March 2011 budget package, requires DOF to reduce each item of appropriation, with the exception of those items for the California State University, Hastings College of the Law, the Legislature, the University of California, and the Judicial Branch, in the total amount of $250 million GF ($163 million other funds) for savings achieved through departmental consolidations, operational efficiencies, and other cost reduction measures, such as reducing contracts.

The May Revision proposal would revise CS 3.91 to identify specific savings of $25.1 million GF ($11.0 million other funds) attributed to a list of departmental consolidations or eliminations identified in the "Reducing State Government" chapter of the May Revision document. The May Revision identifies an additional $16.4 million GF ($30.2 million other funds) from other operational efficiencies. The remaining savings, $208.5 million GF ($121.8 million other funds), would be achieved as proposed in the March 2011 budget package.

CS 13.25 is intended to serve as the mechanism for DOF to adjust budgets upwards, should the Legislature approve certain consolidations or other reductions that require such an action. For instance, should the Legislature approve the elimination of the Fair Employment and Housing Commission (discussed as Issue 2 below), certain functions and responsibilities would be moved to the Department of Fair Employment and Housing and that department's budget would need to be adjusted upwards.

Staff Comment. These control sections are the most effective budgetary process available at present to accomplish this task of reducing state government. Through the control sections, the DOF is given the authority to make necessary budget adjustments consistent with legislative approval. However, it is important to strike an appropriate balance and to ensure that, if the Legislature rejects some of the proposals to reduce state government, those proposals are not then adopted through the control section mechanism. In addition, the current wording of CS 13.25 is not clear as to the Administration's intent (to adjust certain budget items upwards). All of these issues can be addressed going forward; staff, therefore, recommends that the Subcommittee approve these control sections on a placeholder basis, pending further language refinements and to accommodate the work of the other budget Subcommittees who are considering reduction proposals in hearings that either occurred yesterday, are happening today or are happening tomorrow. In addition, staff recommends that the Subcommittee approve Supplemental Report Language to provide greater clarity as to legislative intent and action on the May Revision "Reducing State Government" proposals.

Staff Recommendation: Approve Control Sections 3.91 and 13.25 on a placeholder basis, along with placeholder Supplemental Report Language, pending further language refinements and to incorporate the actions of the other budget subcommittees on the May Revision proposals.

Vote: Staff recommendation approved by a 3-0 vote.

With regard to the SRL, the Subcommittee approved intent language that the DOF examine budgetary costs of boards and commissions including, but not limited to, compensation paid to board and commission members above a $100/day stipend.

Issue 2 – Secretary for State and Consumer Services (0510) GF Budget Reduction and Elimination of Offices of the Insurance Advisor and Privacy Protection

Agency Overview. The State and Consumer Services Agency (SCSA) oversees the departments of Consumer Affairs, Fair Employment and Housing, and General Services. The Agency also oversees the California Science Center, the California African American Museum, the Seismic Safety Commission, the Fair Employment and Housing Commission, the Franchise Tax Board, the California Building Standards Commission, the State Personnel Board, the California Public Employees' Retirement System, the California State Teachers' Retirement System, the Victim Compensation and Government Claims Board, the Office of Privacy Protection, and the Office of the Insurance Advisor.

The entities under the SCSA are responsible for civil rights enforcement, consumer protection, and the licensing of 2.5 million Californians in more than 240 different professions. Agency entities provide oversight and guidance for the procurement of more than $8.9 billion worth of goods and services; the management and development of state real estate; operation oversight of two state employee pension funds; collection of state taxes; hiring of state employees; adoption of state building standards; and the administration of two state museums. In addition, the Secretary for State and Consumer Services Agency is the Chair of the California Building Standards Commission and the Victim Compensation and Government Claims Board, and operates the Office of Privacy Protection.

Budget Overview. The Governor's May Revise Budget provides 10.1 authorized positions and $1.75 million ($202,000 GF). This is a decrease of $789,000 GF, $250,000 in reimbursements, and 5.2 positions from the January Budget.

Proposal 1: Eliminate General Fund for the Agency

Governor's Request. As part of the May Revision, the Governor requests a decrease of $965,000 all funds ($548,000 GF) in 2011-12. This would eliminate GF support for SCSA and require departments under the SCSA's purview to reimburse the SCSA for operational expenses. This decrease will be offset by an increase of $965,000 from reimbursements in 2011-12.

Background. Reimbursement-based funding is already used by the California Labor and Workforce Development Agency. This model of funding operations is based on the establishment of inter-agency agreements between the Agency and the departments it oversees. DOF has stated that the department budgets would not be increased to accommodate increased expenditures from supporting SCASA operations.

Staff Recommendation: Approve the May Revision request.

Vote: Staff recommendation approved by a 3-0 vote.

Proposal 2: Eliminate Office of Insurance Advisor

Governor's Request. As part of the May Revision, the Governor requests a decrease of $250,000 (reimbursements) and 1.9 personnel years in 2011-12 from the elimination of the Office of Insurance Advisor (OIA).

Background. Following the removal of the Department of Insurance from the administration and the creation of an elected Insurance Commissioner pursuant to Proposition 103, the OIA was established in 1991 in order to provide the Governor's Office with independent policy advice on insurance matters makes policy recommendations on legislation. The OIA tracks, monitors, analyzes and makes policy recommendations on pending legislation affecting various lines of insurance coverage, including: annuities, automobile, bonds, commercial, disability, earthquake, flood, health, homeowners, life, long-term care, and workers' compensation.

Staff Recommendation: Approve the May Revision request.

Vote: Staff recommendation approved by a 3-0 vote.

Proposal 3: Eliminate Office of Privacy Protection

Governor's Request. As part of the May Revision, the Governor requests a decrease of $435,000 all funds ($250,000 General Fund), as well as 3.3 positions in 2011-12, through the elimination of the Office of Privacy Protection (OPP). This would provide half-year funding for OPP, which would allow it to be phased out. The total 2010-11 budget for OPP is $701,000 and seven positions.

Background. The OPP is established in statute to "protect the privacy of individuals' personal information in a manner consistent with the California Constitution by identifying consumer problems in the privacy area and facilitating the development of fair information practices…". The OPP's mission is to be a resource and advocate on privacy issues. In addition to providing information and education for consumers, the OPP also makes privacy practice recommendations to businesses and other organizations. OPP's primary activities include:

- Providing information and assistance to individuals on identity theft and other privacy concerns;
- Educating consumers, businesses, and other organizations on privacy rights and practices;
- Coordination with law enforcement on identity theft, data breach, and other topics; and
- Providing recommendations to organization of privacy policies and practices that promote and protect the interests of California consumers.

Staff Comment. OPP has unique tasks in assisting consumers in understanding and addressing identify theft. Also, OPP is very effective in providing assistance to the Legislature in understanding challenges facing consumers and law enforcement.

Staff Recommendation: Reject the May Revision request and refer the matter to policy committee.

Vote: Staff recommendation approved by a 2-1 vote with Senator LaMalfa voting no.

Issue 3 – Secretary for Business, Transportation, and Housing (0520) Decrease State Matching Funds for Tourism Office

Governor's Request. As part of the May Revision, the Governor requests a decrease of $734,000 GF in 2011-12 for the Tourism Office.

Background. The California Office of Tourism works closely with the California Travel and Tourism Commission (CTTC) (a 501 c (6) non-profit organization) with the mission to develop and maintain marketing programs, in partnership with the state's travel industry, to promote the State of California as a premier travel destination.

The CTTC is funded primarily through assessments to businesses in the travel and tourism industry (Accommodations, Restaurant and Retail, Attractions, Transportation and Travel Industry, Passenger Car Rental Industry). These assessments are self-imposed and are renewed every six years, with the next renewal coming in 2013. In addition to the assessment fees, the CTTC also receives a total of $934,000 from the State General Fund to fund some of the Commission's marketing activities.

Staff Comment: The May Revision proposal would reduce General Fund support from $934,000 to $200,000 – enough to maintain the public-private partnership and support the Executive Director. The tourism industry would continue to support the marketing of California tourism through $50 million in industry self-assessed fees.

Staff Recommendation: Approve May Revision request.

Vote: Staff recommendation approved by a 3-0 vote.

Issue 4 – Fair Employment and Housing Commission (1705) Eliminate the Fair Employment and Housing Commission

Governor's Request. As part of the May Revision, the Governor requests to eliminate the Fair Employment and Housing Commission (FEHC), with adjudication of employment and housing discrimination cases instead appealed to the Director of the Department of Fair Employment and Housing (DFEH) beginning January 1, 2012, effectively consolidating workload for savings of $438,000 ($344,000 GF) and 1.4 personnel years in 2011-12. This request includes proposed budget trailer bill language.

Background. The FEHC is a quasi-judicial administrative agency which enforces state civil rights laws regarding discrimination in employment, housing, and public accommodations; pregnancy disability leave; family and medical leave; and hate violence. The FEHC is comprised of seven members, appointed by the Governor and confirmed by the Senate. Members receive $100/day per diem. In 2010-11, the FEHC was budgeted at $1.2 million ($1.034 million GF) and 5.2 authorized positions. The chart below displays the 2010 FEHC case adjudication statistics:

2010 FEHC Case Adjudication Statistics

Accusations Filed by DFEH	59
Hearings calendared by FEHC for three day evidentiary hearings	55
Evidentiary hearings (number of hearings/number of hearing days)	14/29
Case Management Conferences	29
Early Mediation Evaluation Conferences	39
Settlement Conferences/Mediations with Commissioners & staff	6

As part of its proposal to eliminate the FEHC, the Administration indicates that it will consult with stakeholders and evaluate options to phase out the stand-alone FEHC that handles these cases by January 1, 2012. Under the "phase out" plan, the DFEH will employ administrative law judges and, instead of the Commission deciding cases, DFEH's Director (or his/her designee) will decide the case. Rules to interpret the Fair Employment and Housing Act will be issued by DFEH following the current public rule-making process.

Staff Comment. In considering this request, staff notes that a key issue is the adjudicative process and the retention of an entity that can effectively enforce the state's civil rights laws. More specifically, the transition must be done in a precise way to ensure that the FEHC's adjudicatory and regulatory responsibilities are transferred properly, taking into consideration potential conflicts between prosecuting cases (currently through the DFEH) and adjudicating these cases (currently through the FEHC). This request is also accompanied by lengthy budget trailer bill language. As such, and in considering this request, the Subcommittee may wish to refer this proposal to the Senate Judiciary and Transportation and Housing Committees for further review of its impacts as well as potential new approaches.

Staff Recommendation: Reject the May Revision request and and refer the matter to policy committee.

Vote: Staff recommendation approved by a 2-1 vote, with Senator LaMalfa voting no.

Issue 5 – Department of Housing and Community Development (2240) Various Budget Reductions

Governor's Request. As part of the May Revision, the Governor requests to reduce the Department of Housing and Community Development's GF budget by a total of $1.168 million and 9.9 positions, as detailed in the below chart. These requests do not include any proposed budget trailer bill language.

	Description	Proposed Reduction	Fund Source
1	Eliminate Housing Policy Funding, within Division of Housing Policy Development	$1.3 million and 8.5 positions	GF
2	Eliminate Preservation Technical Assistance	$35,000	GF
3	Eliminate Redevelopment Housing Funds Oversight	$123,000 and 1.4 positions	GF
4	Eliminate Child Care Monitoring Support	$10,000	GF

General Department and Budget Background. A primary objective of the Department of Housing and Community Development (HCD) is to expand housing opportunities for all Californians. The HCD administers housing finance, economic development, and rehabilitation programs with emphasis on meeting the shelter needs of low-income persons and families, and other special needs groups. HCD also administers and implements building codes, manages mobilehome registration and titling, and enforces construction standards for mobilehomes. The January Governor's Budget provides the HCD 598.6 authorized positions and $256.0 million ($8.8 million GF). This is a decrease of 6.5 positions and $490.0 million (the majority of the HCD's expenditures are supported by general obligation bond revenue). Therefore, HCD's budget has been steadily decreasing in recent years due to the pending exhaustion of housing bond funds.

Proposal 1: Eliminate Housing Policy Funding

Background. This proposal would eliminate $1.3 million GF and 8.5 positions that support housing policy in the HCD Division of Housing Policy Development (HPD). HPD identifies California's housing needs and develops policies to meet those needs. HPD administers state housing element law, including the review of local general plan housing elements. HCD reports that administering the state's housing element law is the biggest workload driver in HPD. This reduction would decrease HPD's 2011-12 staffing level from 12.5 to 3.5 positions. With that reduced level of staff, HPD would be unable to meet its current workload and would have to ratchet down workload to meet the limited resources available.

The remaining 3.5 positions would be funded as follows: (1) $98,000 from the Air Pollution Control Fund; (2) $1.068 million from the Housing Related Parks program – this resource actually funds a total of seven positions, two of which are assigned to housing element workload; and (3) $136,000 from reimbursements funding from the HCD Division of Financial Assistance (DFA) in recognition of support to DFA programs by HPD.

Staff Comment. HCD review of housing elements has proven critical to ensuring cities and counties create opportunities (zoned land, funding, etc.) for affordable housing. Without that effort on the part of HCD, it does not appear there is another viable method to ensure compliance with housing element law. As such, the LAO is currently providing technical assistance to staff to determine the viability of alternative funding sources to support HPD's housing element-related workload. Three potential fund sources are: (1) Proposition 84; (2) Housing-Related Parks Bond (Propositions 1C and 46); and/or, (3) Proposition 46 Building Equity and Growth in Neighborhoods (BEGIN). As noted above, HRP funds currently provide support for two of the HPD's positions.

Staff Recommendation. Approve the May Revision request contingent on the identification of an alternative fund source to support housing element workload in the Housing Policy Division.

Vote: Staff recommendation approved by a 3-0 vote.

Proposal 2: Eliminate Preservation Technical Assistance

Background. This proposal would eliminate $35,000 GF utilized to provide assistance in the prevention of subsidized housing converting to market rents upon the expiration of the subsidy period. On an annual basis, HCD has awarded a contract totaling $65,000 ($35,000 GF and $30,000 other funds) for this work.

HCD estimates that 78,503 affordable homes are determined to be at-risk of conversion by private owners over the next five years. Because it generally costs half as much and takes half the time to maintain existing affordable housing than building it new, HCD contracts with the California Housing Partnership Corp. (CHPC) to provide technical assistance on preservation issues both with project sponsors as well as to provide technical assistance to persons in preparing local housing elements that are required to include inventories of, and programs for preserving, at-risk properties. These inventories identify at-risk projects with expiring Section 8 contracts and/or federal, state or local subsidized or below market mortgages eligible for prepayment within five years of the term expiration.

HCD indicates that the CHPC investigates the status of potentially at-risk projects by utilizing specific project information from its database, contacts property owners to determine their intentions, and uses its statewide network to identify a preservation purchaser.

Staff Comment. Notwithstanding the merits of providing preservation technical assistance, it is not clear to staff why this should be a state GF cost. It is also not clear why the GF costs could not be supported by federal funds, since a great number of the state's affordable housing units are federally-subsidized and in the Section 8 program. Therefore, staff recommends the Subcommittee approve this request.

Staff Recommendation. Approve the May Revision request.

Vote: Staff recommendation approved by a 3-0 vote.

Proposal 3: Eliminate Redevelopment Housing Funds Oversight

Background. This proposal would eliminate $123,000 GF and 1.4 positions that support HCD oversight of redevelopment agency (RDA) low- and moderate-income housing funds and an annual report on housing funds and activities.

Staff Comment. Staff notes that the primary function here is the compiling of a report of the reports submitted by RDAs. The Administration indicates that this proposal is consistent with the broader proposal to eliminate RDAs. Staff also notes that under current law RDAs are required to submit annual financial transaction and compensation reports to the State Controller's Office.

Staff Recommendation. Approve the May Revision request.

Vote: Staff recommendation approved by a 3-0 vote.

Proposal 4: Eliminate Child Care Monitoring Support

Background. This proposal would eliminate $10,000 GF for child care monitoring support. Prior to 2004-05, HCD administered two GF-funded funds that were intended to provide loans and loan guarantees for private child care centers. In 2004-05, the Budget Act transferred the remaining money from those funds back to the GF, but the funds themselves were not abolished. In 2009, the funds were abolished as part of the general government budget trailer bill. HCD is proposing a state operations reduction of $10,000 GF.

Staff Comment. While it is correct that the state has not made any new awards under this program in many years, the prior awards required a commitment for the child care provider to provide care for an extended period of time. HCD indicates that there are still 14 child care loans outstanding that HCD must administer. The last of these loans have a payoff in 2033. Staff notes that $10,000 in funding would provide support for roughly 0.1 percent of one position. As such, this workload would appear to be absorbable within existing resources.

Staff Recommendation: Approve the May Revision request.

Vote: Staff recommendation approved by a 3-0 vote.

Issue 6 – Commission on the Status of Women (8820) Elimination of the Commission on the Status of Women

Department Overview. The Commission on the Status of Women (CSW) is an independent, non-partisan agency working to advance the causes of women. Toward that end, the CSW influences public policy by advising the Governor and the Legislature on issues impacting women and educating and informing its constituencies-thereby providing opportunities that empower women and girls to make their maximum contribution to society. The CSW consists of a 17-member body including the Superintendent of Public Instruction, the Labor Commissioner, three Assembly members and three Senators. Nine of the 17 members are public members: one appointed by the Speaker of the Assembly; one by the Senate Committee on Rules; and seven are appointed by the Governor. Public members serve four-year terms and are reimbursed for necessary expenses.

Budget Overview. The Governor's January Budget provided the CSW with $467,000 total funds ($464,000 GF and $2,000 reimbursements) and 4.3 positions.

Governor's Request. As part of the May Revision, the Governor requests a decrease of $234,000 all funds ($233,000 GF) and 2.1 personnel years in 2011-12 in order to eliminate the CSW.

Background. The Governor's justification for the elimination of the CSW is that there are numerous formal and informal avenues for the Governor and Legislature to seek advice on public policy issues impacting women. However, the CSW has many unique tasks. The CSW is the only state agency that looks specifically at all issues impacting women. The CSW holds public hearings across the state to gather input on issues important to women, and uses that information to develop a public policy agenda. Also, the CSW provides the Legislature, Governor, and advocates with gender analysis on proposed bills and actions. On its website, CSW provides a wide variety of information and resources on issues impacting women and girls. Also, CSW facilitates the development of coalitions of diverse organizations around various issues such as reproductive rights, paid family leave, incarcerated women, etc.

Staff Recommendation: Reject the May Revision request and refer the matter to policy committee.

Vote: Staff recommendation approved by a 2-1 vote with Senator LaMalfa voting no.

Issue 7 – Department of Finance (8860) Accelerate the End of the California Recovery Task Force

Governor's Request. As part of the May Revision, the Governor requests to eliminate the California Recovery Task Force by January 1, 2012, for savings of $0.8 ($0.4 million GF and $0.4 million Central Service Cost Recovery Fund) and 3.4 positions. This request does not include any proposed budget trailer bill language.

Background. On February 17, 2009, President Obama signed the American Recovery and Reinvestment Act (ARRA), a $787 billion federally-funded economic stimulus plan for a wide range of federal, state, and local programs as well as tax relief for qualified businesses and individuals. ARRA also created new requirements for state-level oversight and reporting of stimulus dollars provided to state entities. Both the 2009-10 and 2010-11 budgets provided funding for California's ARRA accountability framework, comprised of four organizational components: the California Recovery Task Force (CRTF); the ARRA Inspector General (ARRA IG); the Bureau of State Audits (BSA); and, the State Controller's Office (SCO). Both the BSA and SCO were pre-existing entities, while the CRTF and ARRA IG were established via Executive Order by the Governor in Spring 2009. In January 2011, Governor Brown announced he was eliminating the ARRA IG's Office six months early (funding for that office in the 2010-11 budget was provided on a one-year limited-term basis). Any outstanding audit activities of that office were transferred to the SCO or BSA.

Building on a legislative action in the March 2011 budget package, which reduced the California Recovery Task Force by $393,000 ($224,000 GF and $169,000 Central Service Cost Recovery Fund), the May Revision proposes to eliminate the Task Force on January 1, 2012, for additional savings of $800,000 ($400,000 GF) and 3.4 positions. Under the May Revision proposal, any remaining federally-mandated quarterly reporting will be decentralized to the appropriate state department.

Staff Recommendation: Approve the May Revision request.

Vote: Approved modified staff recommendation by a 3-0 vote, as follows: approved the portion of the May Revision request that is additive to the action the Legislature already adopted as part of the March 2011 Budget package to reduce 2011-12 funds for the Task Force by $393,000 ($224,000 GF and $169,000 Central Service Cost Recovery Fund).